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No. 16105 VOL. 3089

United States Court of Appeals for the Ninth Circuit

RICHARD C. HOY, as District Director of the Immigration and Naturalization Service, Los Angeles, California, Appellant,

vs.

ARNULFO ROJAS-GUTIERREZ, Appellee.

Transcript of Record

Appeal from the United States District Court for the Southern District of California, Central Division

FILED
SEP 3 - 1958
PAUL P. O'BRIEN, CLERK

Phillips & Van Orden Co., Fourth and Berry Sts., San Francisco, Calif.—8-27-58

No. 16105

United States Court of Appeals

for the Ninth Circuit

RICHARD C. HOY, as District Director of the Immigration and Naturalization Service, Los Angeles, California, Appellant,

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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For Appellee:

NEWMAN AND NEWMAN,
PHILIP M. NEWMAN,

354 South Spring Street,
Los Angeles 13, California. [1]*

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* Page numbers appearing at bottom of page of Original Transcript of Record.

In the United States District Court, Southern District of California, Central Division

No. 1152-57 WM

ARNULFO ROJAS-GUTIERREZ, Plaintiff,

vs.

ALBERT DEL GUERCIO, as District Director of the Immigration and Naturalization Service, Los Angeles, California.

PETITION FOR JUDICIAL REVIEW AND DECLARATORY JUDGMENT: INJUNCTION

Plaintiff alleges:

I.

That this action arises out of, and is based on the Declaratory Judgment Act (28 U.S.C.A. 2201) and Section 10 of the Administrative Procedure Act (5 U.S.C.A. 1009) (60 Stat. 243).

II.

That the plaintiff is a resident of the County of Los Angeles, State of California.

III.

That the defendant is the District Director of the Immigration and Naturalization Service, Department of Justice, at Los Angeles, California.

IV.

That the plaintiff was the subject of deportation

proceedings before the Immigration and Naturalization Service in Los Angeles, California, which were based on a warrant charging that [2] the plaintiff had been convicted of the crime of burglary prior to his entry into the United States.

That these deportation proceedings were terminated by an order entered by the Assistant Commissioner of Immigration on May 4, 1940 which found the plaintiff not to be deportable.

V.

That the plaintiff was again the subject of deportation proceedings instituted on February 10, 1953 charging the plaintiff with being subject to deportation under Section 241 (a) (11) of the Immigration and Naturalization Act of 1952, in that he had been convicted of a law or regulation relating to the illicit traffic in narcotic drugs (marihuana).

VI.

That on May 12, 1955, the plaintiff filed a petition for naturalization at the office of the Immigration and Naturalization Service, Los Angeles, California.

VII.

That on July 18, 1956 Section 241 (a) (11) of the Immigration and Naturalization Act of 1952 was amended by Public Law 728, 84th Congress (78 Stat. 575) to provide in effect and substance for the deportation of an alien who at any time has been convicted of a violation of, or conspiracy to violate, any law or regulation relating to the illicit possession of, or traffic in narcotic drugs.

VIII.

That on September 28, 1956, the plaintiff was served with an Order to Show Cause by the Immigration and Naturalization Service ordering the plaintiff to Show Cause why he should not be deported from the United States on the charge that he had been convicted of a violation of law relating to the illicit possession of narcotic drugs in violation of Section 241 (a) (11) of the Immigration and Naturalization Act of 1952 as amended. [3]

IX.

That on October 19, 1956 after a hearing, a Special Inquiry Office of the Immigration and Naturalization Service, acting as aforesaid, ordered that the plaintiff be deported from the United States on the charge contained in the Order to Show Cause.

X.

That on March 7, 1957, the Board of Immigration Appeals, United States Department of Justice affirmed the decision of the Special Inquiry Office and dismissed the appeal of the plaintiff.

XI.

That on or about the 25th day of September, 1957 the defendant, acting as aforesaid, and through his subordinates, ordered plaintiff to report to the office of the United States Immigration and Naturalization Service, Department of Justice, for deportation from the United States.

XII.

That by the Order of the Assistant Commissioner of Immigration on May 4, 1948, the plaintiff acquired a status of a non-deportable resident alien and that said status was preserved by Section 405 (a) of the Immigration and Naturalization Act of 1952 (U.S.C.A.) and plaintiff cannot be deprived of said status by the statute relied upon by the defendant for the outstanding order of deportation against the plaintiff.

XIII.

That by the order of the Board of Immigration Appeals on December 2, 1953 terminating deportation proceedings against the plaintiff and therefore holding him to be non-deportable, the plaintiff acquired a status of a non-deportable resident alien, that said status was preserved by Section 405 (a) of the Immigration and Naturalization Act of 1952 and that plaintiff cannot be deprived of the status by the statute relied upon by the defendant for the outstanding order of deportation against the [4] plaintiff.

XIV.

That upon filing a petition for naturalization on May 12, 1955, the plaintiff had a right in the process of acquisition within the provisions of Sections 405 (a) and 405 (b) of the Immigration and Naturalization Act of 1952 that cannot be affected or taken away by the statute relied upon by defendant for the outstanding order of deportation against plaintiff.

XV.

That the order of deportation that is outstanding against the plaintiff issued as aforesaid, is in violation of the provisions of Section 405 (a) of the Immigration and Naturalization Act of 1952 (8 U.S.C.A.) and illegal.

XVI.

That all administrative remedies available to this plaintiff in this matter have been exhausted.

For a Second and Special Cause of Action, the plaintiff alleges:

I.

That plaintiff repleads paragraphs I, II, III, VIII, IX, X, XI, and XVI and incorporated same by reference as if repleaded in this cause of action.

II.

That the order of deportation issued against plaintiff by the defendant on or about September 25, 1957 is based upon an erroneous application of Section 241 (a) (11) of the Immigration and Naturalization Act of 1952 as amended in that said section provides for the deportation of an alien who at any time has been convicted of a violation of any law or regulation relating to the illicit possession of narcotic drugs, when in fact the conviction of this plaintiff to which the order refers except for the possession of marihuana which is not included in this [5] Section under the term narcotic drugs.

III.

That the order of defendant is, therefore, illegal as the conviction as aforesaid is not within the provisions of the Section cited.

Wherefore, plaintiff prays for judgment against defendant:

1. Declaring the order of deportation against the plaintiff to be contrary to law.

2. Enjoining the defendant from proceeding with the deportation of plaintiff under the outstanding order.

NEWMAN & NEWMAN,
/s/ By PHILIP M. NEWMAN. [6]

Duly Verified. [7]

[Endorsed]: Filed October 2, 1957.

[Title of District Court and Cause.]

ANSWER

Comes Now the defendant, Albert Del Guercio, as District Director of the Los Angeles District, Immigration and Naturalization Service, and in answer to plaintiff's complaint and petition for review, declaratory judgment and injunction on file herein, admits, denies and alleges as follows:

I.

Referring to the allegations contained in para-

graph I of plaintiff's complaint, neither admits nor denies the same, said allegations being conclusions of law.

II.

Defendant alleges that he is without knowledge or information sufficient to form a belief as to the truth of the allegation contained in paragraph II.

III.

Defendant admits the allegations contained in paragraph III. [8]

IV.

Defendant admits allegations contained in paragraph IV, except that defendant denies that the order entered by the Assistant Commissioner of Immigration which found the plaintiff not to be deportable was made on May 4, 1940; rather, defendant alleges that such order was entered on May 4, 1948.

V.

Defendant admits the allegations contained in paragraph V. Defendant alleges that on November 2, 1953, the Special Inquiry Officer in such proceedings ordered plaintiff's deportation, but that on December 2, 1953, the Board of Immigration Appeals terminated such Order on the grounds that a conviction for possession of narcotic drugs did not constitute a deportation charge (at that time).

VI.

Defendant admits the allegations contained in paragraph VI.

VII.

Defendant admits the allegations contained in paragraph VII.

VIII.

Defendant admits the allegations contained in paragraph VIII.

IX.

Defendant admits the allegations contained in paragraph IX.

X.

Defendant admits the allegations contained in paragraph X.

XI.

Defendant admits the allegations contained in paragraph XI. However, defendant alleges that, upon the filing of the instant petition, defendant has not and does not intend to take any action to remove plaintiff from the jurisdiction of this Court.

XII.

Defendant denies each and every allegation contained in paragraph XII. [9]

XIII.

Defendant denies each and every allegation contained in paragraph XIII.

XIV.

Defendant denies each and every allegation contained in paragraph XIV.

XV.

Defendant denies each and every allegation contained in paragraph XV.

XVI.

Defendant admits the allegation contained in paragraph XVI. Defendant, in answer to paragraph I of plaintiff's second cause of action, refers to paragraphs I, II, III, VIII, IX, X, XI and XVI of this Answer and incorporates such paragraphs by reference as if herein repleaded.

XVII.

Defendant denies each and every allegation contained in paragraph II of plaintiff's second cause of action.

XVIII.

Defendant denies each and every allegation contained in paragraph III of plaintiff's second cause of action.

Wherefore, defendant prays that plaintiff take nothing by reason of his complaint, that the Court find the Order of Deportation valid and enforceable, and for such other and further relief as to the Court seems proper.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief, Civil Division,

/s/ MARY G. CREUTZ,
Assistant U. S. Attorney,
Attorneys for Defendant. [10]

Affidavit of Service by Mail Attached. [11]

[Endorsed]: Filed December 2, 1957.

PLAINTIFF'S EXHIBIT No. 1

[Title of District Court and Cause.]

PRE-TRIAL ORDER

The following admissions and agreements of fact are hereby made by the parties of this matter and require no proof:

(1) That in 1948 the plaintiff was the subject of deportation proceedings before the Immigration and Naturalization Service in Los Angeles, California, said proceedings having been based on the charge that the plaintiff had been convicted of the crime of burglary prior to an entry into the United States of America; that on May 4, 1948, the Commissioner of Immigration ordered these proceedings terminated and found the plaintiff not to be deportable.

(2) That in 1953 plaintiff was the subject of deportation proceedings before the Immigration and Naturalization Service which were based upon the convictions of the plaintiff on March 11, 1938, November 13, 1945, and April 8, 1949 for violations of Section 11,160 and 11,500 of the Health

Plaintiff's Exhibit No. 1—(Continued)

& Safety Code of the State of California; that on December 2, 1953, the Board of Immigration Appeals held the plaintiff was non-deportable on these charges and ordered the proceedings terminated.

(3) That on May 12, 1955 the plaintiff herein filed a petition for naturalization with the Immigration and Naturalization Service of Los Angeles, California.

(4) That on July 18, 1956, Section 241 (a) (11) of the Immigration Nationality Act of 1952 (8 U.S.C.A. 1251) (11) was amended to provide in effect and substance for the deportation of an alien who at any time has been convicted of a violation of or conspiracy to violate any law or regulations relating to the illicit possession of, or traffic in narcotic drugs;

(5) That on September 28, 1956 the Immigration and Naturalization Service instituted deportation proceedings against the plaintiff herein;

(6) That on October 19, 1956 after a hearing, a Special Immigration Office of the Immigration and Naturalization Service ordered that the plaintiff be deported from the United States on the charges that he had been convicted of the violations of the Section 11,160 and 11,500 of the Health and Safety Code of the State of California as aforesaid; said Order of deportation being based on Section 241 (a) (11) of the Immigration Nationality Act of 1952 as amended on July 18, 1956 (8 U.S.C.A. 1251) (a) (11); that on March 7, 1957

Plaintiff's Exhibit No. 1—(Continued)

the Board of Immigration Appeals affirmed said order of deportation against the plaintiff and dismissed the appeal of the plaintiff.

(7) That on September 25, 1957, the Immigration and Naturalization Service of Los Angeles, California ordered the plaintiff to report to their office for deportation from the United States of America.

(8) That the plaintiff's convictions by the Superior Court of the State of California in and for the County of Los Angeles on March 11, 1938, November 13, 1945, and on April 8, 1949 of having in his possession the flowering tops and leaves of Indian hemp (Cannabis Sativa) (Marihuana) under the provisions of Section 11,160 and 11,500 of the Health and Safety Code of the State of California.

(9) That on July 18, 1956, Section 241 (a) (11) of the Immigration and Nationality Act of 1952 (8 U.S.C.A. 1251) (a) (11) was amended, effective July 19, 1956, to provide in effect and substance for the deportation of an alien who at any time had been convicted of a violation of, or conspiracy to violate, any law or regulation relating "to the illicit possession of or traffic in narcotic drugs * * *"

(10) That Richard C. Hoy be substituted in place of Albert del Guercio as the defendant in this matter.

Issues of Law

1. Whether the plaintiff herein acquired a status of non-deportability by virtue of the decisions of

Plaintiff's Exhibit No. 1—(Continued)

the Commissioner of Immigration on May 4, 1948 and the Board of Immigration Appeals on December 2, 1953.

2. Whether by filing a petition for naturalization on May 12, 1955 the plaintiff herein had a right in process of acquisition.

3. If the plaintiff acquired a status of non-deportability by virtue of the decision referred to above, whether such status was preserved by the Savings Clause (Section 405) (a) and (b) of the Immigration and Nationality Act of 1952 and the plaintiff cannot be deprived of said status by the amendment of Section 241 (a) (11) of the Immigration and Nationality Act of 1952 (8 U.S.C.A. 1251) (11).

4. If the plaintiff herein had a right in the possession of acquisition by the filing of his naturalization petition on May 12, 1955 and whether that right was preserved by Section 405 (a) and (b) of the Immigration and Nationality Act of 1952 (8 U.S.C.A. 1251).

5. Whether Section 241 (a) (11) of the Immigration and Nationality Act of 1952 as amended (8 U.S.C.A. 1251) (a) (11) as amended includes the substance known as marihuana a "narcotic drug" when referring to "illicit possession of or traffic in narcotic drugs * * *".

Issues of Fact: None

The foregoing admissions of fact have been made

Plaintiff's Exhibit No. 1—(Continued)

by the parties in open court at the pre-trial conference; and issues of fact and law being thereupon stated and agreed to, the Court makes this Order which shall govern the course of the trial unless modified.

Dated: March 3, 1958.

The foregoing pre-trial Order is hereby approved:

NEWMAN & NEWMAN,
/s/ By PHILIP M. NEWMAN,
Attorneys for Plaintiff.

/s/ MARY G. CREUTZ,
Attorneys for Defendant.

March 3, 1958.

/s/ WM. C. MATHES,
Judge of the U. S. District Court.

[Endorsed]: Filed March 3, 1958.

[Title of District Court and Cause.]

MEMORANDUM OF DECISION

Appearances: Messrs. Newman & Newman and Philip M. Newman, 354 South Spring Street, Los Angeles 13, California, Attorneys for Plaintiff. Laughlin E. Waters, United States Attorney, Rich-

ard A. Lavine, Assistant U. S. Attorney, Mary G. Creutz, Assistant U. S. Attorney, 600 Federal Building, Los Angeles 12, California, Attorneys for Defendant. [12]

Mathes, District Judge:

Plaintiff, an alien of Mexican nationality, has invoked the jurisdiction of this Court under § 10 of the Administrative Procedure Act [60 Stat. 243 (1946), 5 U.S.C. § 1009] to review administrative proceedings had before the Immigation and Naturalization Service of the Department of Justice which resulted in a final order of the Attorney General that plaintiff be deported from the United States. [See Shaughnessy v. Pedreiro, 349 U.S. 48 (1955); cf. Kessler v. Strecker, 307 U.S. 22, 34-35 (1939).]

The case has been submitted for decision upon an agreed statement of facts set forth in the pre-trial conference order. In 1948 plaintiff was before the Immigration and Naturalization Service in deportation proceedings based upon the charge that prior to entry into the United States he had been convicted of the crime of burglary. On May 4, 1948, the Commissioner of Immigration found plaintiff not to be deportable and ordered the deportation proceedings terminated.

In 1953 plaintiff was again the subject of deportation proceedings, this time based upon his conviction in 1938, 1945, and 1949 of the crime of possessing marihuana in violation of §§ 11001, 11160 and 11500 of the California Health and Safety Code. On December 2, 1953, the Board of Immi-

gration Appeals [13] held that plaintiff was not deportable because of these convictions and ordered the 1953 deportation proceedings terminated.

Almost two years later, in 1955, plaintiff filed a petition for naturalization at the Los Angeles office of the Immigration and Naturalization Service.

On July 18, 1956, § 241(a)(11) of the Immigration and Nationality Act of 1952 was amended to declare deportable any alien "who at any time has been convicted of a violation of * * * any law or regulation relating to the illicit possession of * * * narcotic drugs * * *" [70 Stat 575 (1956), 8 U.S.C. §2151(a)(11) (Supp. V, 1958).]

Shortly thereafter, on September 28, 1956, the Immigration and Naturalization Service commenced the deportation proceedings under review in this action by ordering plaintiff to show cause why he should not be deported from the United States by reason of having been convicted in 1938, 1945, and 1949 of unlawful possession of "parts of the plant Cannabis Sativa L. (commonly known as marihuana)" in violation of §§ 11001, 11160 and 11500 of the Health and Safety Code of California.

A hearing was had before a Special Inquiry Officer [8 U.S.C. § 1252(b)], who found plaintiff to be a deportable alien under the above-quoted amendment to § 241(a)(11) of the [14] Immigration and Nationality Act of 1952 [8 U.S.C. § 1251 (a)(11) (Supp. V, 1958)], and on October 19, 1956, ordered him deported. The Board of Immigration Appeals affirmed the order of deportation. And on September 25, 1957, defendant directed

plaintiff to report to the Los Angeles office of the Immigration and Naturalization Service for deportation. This action followed, resulting in administrative suspension of deportation pending judicial review.

Plaintiff advances three grounds in support of his contention that the deportation order of October 19, 1956, is without authority in law and should be declared a nullity:

First, that convictions of unlawful possession of marihuana are not convictions of "illicit possession of narcotic drugs" within the meaning of the 1956 amendment to § 241(a)(11) of the Immigration and Nationality Act of 1952 [8 U.S.C. § 1251(a)(11) (Supp. V, 1958)];

Second, that even if otherwise deportable under the 1956 amendment to § 241(a)(11), plaintiff's deportation is precluded by the existence of a "right in process of acquisition" under his pending petition for naturalization filed in 1955, which right was preserved by the saving clauses set forth in § 405(a) and (b) of the Immigration and Nationality Act of 1952 [66 Stat. 280 (1952), 8 U.S.C. note foll. § 1101; cf. Shomberg v. United States, 348 U.S. 540 (1955)]; and [15]

Third, that in all events plaintiff acquired a "status of non-deportability" by virtue of the administrative decisions dismissing the 1948 and 1953 deportation proceedings against him, and this claimed status was preserved over the 1956 amendment to § 241(a)(11) by the saving clauses in § 405 (a) and (b) of the Act. [See Mulcahey v. Catala-

notte, 353 U.S. 692 (1957); cf. Lehmann v. United States ex rel Carson, 353 U.S. 685 (1957).]

Turning to the first contention, plaintiff urges that marihuana is not a "narcotic drug" within the meaning of § 241(a)(11), as amended in 1956, since the Congress, apparently bearing in mind the question whether marihuana possesses the habit-forming qualities of substances generally classified as narcotic drugs, has not seen fit expressly to include marihuana in that category. In this connection it is noted that marihuana was treated separately from "narcotic drugs" in the Narcotic Control Act of 1956 [70 Stat. 567 (1956)], enacted by the same Congress that enacted the 1956 amendment to § 241(a)(11) of the Immigration and Nationality Act of 1952. [See U. S. Code Cong. and Ad. News pp. 3321, 3274-3322 (1956).]

However, it is unnecessary here to reach the problem whether marihuana is a "narcotic drug" within the meaning of § 241(a)(11), for I find, as plaintiff asserts and defendant concedes, that my brother Judge Westover has already explored [16] the question and reached a conclusion which accords with plaintiff's contention here—namely, that marihuana is not a narcotic drug within the meaning of the statute in question. [See Manuel Mendoza-Rivera v. Del Guercio, ... F. Supp. .... (S.D. Cal. 1958), Civil No. 813-57 HW, decided February 24, 1958.]

The Court of Appeals of this Circuit has quoted with approval the proposition stated in Shreve v. Cheesman, 69 Fed. 785, 791 (8th Cir. 1895), cert.

denied, 163 U.S. 704 (1896), that the "various judges who sit in the same court should not attempt to overrule the decisions of each other * * * except for the most cogent reasons." [Carnegie Nat. Bank v. City of Wolf Point, 110 F. 2d 569, 573 (9th Cir. 1940).]

For judges of co-ordinate jurisdiction to presume to overrule one another usually adds only unseemly conflict and confusion where certainty and predictability are most to be desired. The "overruling" decision settles nothing, and more often than not serves only to compound uncertainty as to the correct rule to be followed. The reasons so well put by Judge Sanborn more than a half-century ago in Shreve v. Cheesman, supra, a fortiori apply today. [See 69 Fed. at 790-791; also TCF Film Corp. v. Gourley, 240 F. 2d 711 (3rd Cir. 1957).]

Unless a judge can say that he thinks a decision of [17] a colleague is on the face of it patently erroneous, he should follow it. Especially is this true of decisions in the same case, and of decisions in different cases involving rules of practice and procedure or rules of property or, as here, the status of persons. [Cf.: Dictograph Products Co. v. Sonotone Corp., 230 F. 2d 131 (2d Cir. 1956); TCF Film Corp. v. Gourley, supra, 240 F. 2d 711.]

In the days when Justices of the Supreme Court "rode the circuit" and presided in the trial courts, Mr. Justice Field, sitting as Circuit Justice in the then Circuit Court of the District of Nevada, upon being importuned to dissolve an injunction which

had been issued by the circuit judge, wrote: "I could not with propriety reconsider his decision, even if I differed from him in opinion. The circuit judge possesses * * * equal authority with myself in the Circuit, and it would lead to unseemly conflicts, if the rulings of one judge, upon a question of law, should be disregarded, or be open to review by the other judge in the same case." [Cole Silver Min. Co. v. Virginia & Gold Hill Water Co., 6 Fed. Cas. 72, 74, No. 2990 (C.C.D. Nev. 1871).]

Since I cannot say that on the face of it Judge Westover's conclusion on the question of law now presented appears to me to be patently erroneous, I follow it without further study. Anyone who wishes to challenge that ruling [18] should do so in the Court of Appeals, which was established to correct errors of the Judges of this Court.

What has been said is not to intimate that I tend to disagree with, or even question the soundness of the conclusion Judge Westover has reached, but only to emphasize that, until overruled, I feel in comity bound to follow his ruling on this question of statutory construction, and this without myself re-examining the problem.

However, defendant points to the fact that the decision of my brother Chief Judge Yankwich in United States v. Ford Coupe Automobile, 83 F. Supp. 866 (S.D. Cal. 1949), rules marihuana to be a narcotic drug. This presents a dilemma more

apparent than real, since the decision there does not conflict with that of Judge Westover.

The case before Judge Yankwich involved proceedings to declare the forfeiture of an automobile used in transporting a "contraband article". [See 49 U.S.C. §§ 781-788.] And there the statute, after declaring "contraband article" to include "any narcotic drug", in turn expressly defines "narcotic drug" to include "marihuana". [49 U.S.C. §§ 781, 787(d).]

Inasmuch as plaintiff must prevail on the authority of Judge Westover's holding that the term "narcotic drug", as used in the 1956 amendment to § 241(a)(11) of the Immigration [19] and Nationality Act of 1952, does not include marihuana, it is unnecessary to consider the other grounds urged.

For the reasons stated, plaintiff is entitled to judgment (1) annulling the final order of the Attorney General directing that he be deported from the United States, and (2) permanently enjoining defendant from proceeding with deportation by authority of such order.

The attorneys for plaintiff may serve and lodge with the Clerk within ten days findings of fact, conclusions of law and judgment accordingly, to be settled pursuant to Local Rule 7. [20]

[Endorsed]: Filed April 25, 1958.

United States District Court, Southern District of California, Central Division

No. 1152-57 WM

ARNULFO ROJAS-GUTIERREZ,

Plaintiff,

vs.

RICHARD C. HOY, as District Director of the Immigration and Naturalization Service, Los Angeles, California, Defendant.

FINDINGS OF FACTS AND CONCLUSIONS OF LAW AND JUDGMENT

Findings of Facts

I.

That on July 18, 1956, Section 241 (a) (11) of the Immigration & Nationality Act of 1952 was amended to declare deportable any alien "who at any time has been convicted of violation * * * any law or regulation relating to the illicit possession of * * * narcotic drugs * * *" (8 U.S.C. 1251) (a) (11).

II.

That on September 28, 1956, the Immigration & Naturalization Service commenced deportation proceedings against the plaintiff by ordering the plaintiff to show cause why he should not be deported from the United States by reason of having been convicted in 1938, 1945, and 1949 of an unlawful possession of "parts of the plant Can-

nabis Sativa (commonly known as marihuana)" in violation of Sections 11001, 11160, and 11500 of the Health and Safety Code of California. [21]

III.

That a hearing was had before a Special Inquiry Officer of the Immigration & Naturalization Service who found plaintiff to be deportable alien under the above quoted amendment to Section 241 (a) (11) of the Immigration & Nationality Act of 1952 (8 U.S.C. 1251) (a) (11), and on October, 1956, ordered him deported; that the Board of Immigration Appeals affirmed the order of deportation; that on September 25, 1957, defendant directed plaintiff to report to the Los Angeles office of the Immigration & Naturalization Service for deportation.

Conclusions of Law

I.

That the term "narcotic drug" as used in a 1956 amendment to Section 241 (11) of the Immigration & Nationality Act of 1952 as amended (8 U.S.C. 1251) (a) (11) does not include marihuana.

II.

That marihuana is not a narcotic drug within the meaning of the statute in question.

III.

That the plaintiff is not deportable under Section

241 (a) (11) of the Immigration & Nationality Act of 1952 as amended (8 U.S.C. 1251) (11).

IV.

That the plaintiff is entitled to judgment annulling the order of deportation issued by a Special Inquiry Officer of the Immigration and Naturalization Service and annulling the order of the Board of Immigration Appeals dated October 19, 1956, affirming the order of deportation of the Special Inquiry Officer.

V.

That plaintiff is entitled to judgment permanently enjoining the defendant from proceeding with the deportation of the plaintiff by authority of such order. [22]

Judgment

In accordance with the foregoing Findings of Facts and Conclusions of Law, It Is Ordered and Adjudged and Decreed:

1. The order of deportation of the Immigration & Naturalization Service, Department of Justice, directing the deportation of the plaintiff Arnulfo Rojas-Gutierrez is hereby set aside and declared null and void and of no effect.

2. The defendant is permanently enjoined from proceeding with the deportation of the plaintiff by authority of such order.

Dated: May 6, 1958.

/s/ WM. C. MATHES,
Judge, U. S. District Court.

Approved as to form:

/s/ MARY G. CREUTZ,
Assistant U. S. Attorney. [23]

[Endorsed]: Filed May 6, 1958. Entered May 7, 1958.

[Title of District Court and Cause.]

NOTICE OF APPEAL TO COURT OF APPEALS, NINTH CIRCUIT

Notice Is Hereby Given that Richard C. Hoy, defendant above named, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the final judgment entered in this action on May 7, 1958.

Dated: This 9th day of June, 1958.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,
MARY G. CREUTZ,
Assistant U. S. Attorney,
/s/ MARY G. CREUTZ,
Assistant U. S. Attorney,
Attorneys for Defendant. [24]

Affidavit of Service by Mail Attached. [25]

[Endorsed]: Filed June 9, 1958.

[Title of District Court and Cause.]

STIPULATION RE IMMIGRATION FILE NO. A3 548 650 AND ORDER THEREON

It Is Hereby Stipulated by and between counsel for the respective parties hereto that Immigration File No. A3 548 650 admitted in evidence as defendant's Exhibit A, need not be printed in the record on appeal in the above-entitled matter, but may be forwarded to the United States Court of Appeals for the Ninth Circuit in its original form.

Dated: This 1st day of July, 1958.

NEWMAN & NEWMAN,
/s/ By PHILIP M. NEWMAN,
Attorneys for Plaintiff.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,
MARY G. CREUTZ,
Assistant U. S. Attorney, [29]
/s/ MARY G. CREUTZ,
Assistant U. S. Attorney,
Attorneys for Defendant.

It Is So Ordered this 1st day of July, 1958.
/s/ WM. C. MATHES,
U. S. District Judge. [30]

[Endorsed]: Filed July 1, 1958.

[Title of District Court and Cause.]

CERTIFICATE BY CLERK

I, John A. Childress, Clerk of the above-entitled Court, hereby certify that the items listed below constitute the transcript of record on appeal to the United States Court of Appeals for the Ninth Circuit, in the above-entitled matter:

A. The foregoing pages numbered 1 to 30, inclusive, containing the original:

Petition for Judicial Review.

Answer.

Memorandum of Decision.

Findings of Fact, Conclusions of Law and Judgment.

Notice of Appeal.

Designation of Record on Appeal.

Stipulation re: Immigration File A3 548 650 & Order thereon.

B. Plaintiff's Exhibit 1.

Defendant's Exhibit A.

I further certify that my fee for preparing the foregoing record, amounting to $1.60, has not been paid by appellant.

Dated: July 18, 1958.

[Seal] JOHN A. CHILDRESS,
Clerk,

/s/ By WM. A. WHITE,
Deputy Clerk.

[Endorsed]: No. 16105. United States Court of Appeals for the Ninth Circuit. Richard C. Hoy, as District Director of the Immigration and Naturalization Service, Los Angeles, California, Appellant, vs. Arnulfo Rojas-Gutierrez, Appellee. Transcript of Record. Appeal from the United States District Court for the Southern District of California, Central Division.

Filed and Docketed: July 21, 1958.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

In The United States Court of Appeals
For The Ninth Circuit

No. 16105

RICHARD C. HOY, as District Director of the Immigration and Naturalization Service, Los Angeles, California, Appellant,

vs.

ARNULFO ROJAS-GUTIERREZ,
Appellee.

APPELLANT'S STATEMENT OF POINTS ON APPEAL

The appellant hereby designates the following Point on Appeal in the above entitled matter.

I.

Conviction of an alien under California law of unlawful possession of marihuana is a conviction of "illicit possession of * * * narcotic drugs" within the meaning of the 1956 Amendment to Section 241 (a)(11) (8 U.S.C. Sec. 1251(a)(11), Supplement V, 1958) and therefore constitutes a proper ground for deportation thereof.

Dated: This 28th day of July, 1958.

LAUGHLIN E. WATERS,
United States Attorney,

RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief, Civil Division,

/s/ MARY G. CREUTZ,
Assistant U. S. Attorney,
Attorneys for Appellant.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed July 30, 1958. Paul P. O'Brien, Clerk.

[Title of Court of Appeals and Cause.]

APPELLANT'S DESIGNATION OF RECORD TO BE PRINTED

Appellant Hereby Designates the following record to be printed in the above entitled matter:

1. Names and addresses of attorneys.

2. Petition for Judicial Review.
3. Answer.
4. Pre-trial Order (Exhibit 1 in Evidence).
5. Findings of Fact, Conclusions of Law and Judgment.
6. Notice of Appeal.
7. Memorandum of Decision.
8. Designation of Record on Appeal.
9. Stipulation re Immigration File and Order Thereon.
10. Appellant's Statement of Points on Appeal.
11. Appellant's Designation of Record to be Printed.

Counsel for the parties have stipulated that the Exhibits received in evidence might be considered in their original form and need not be printed.

Dated: July 28, 1958.

LAUGHLIN E. WATERS,
United States Attorney,

RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief, Civil Division,

/s/ MARY G. CREUTZ,
Assistant U. S. Attorney,
Attorneys for Appellant.

Affidavit of Service By Mail Attached.

[Endorsed]: Filed July 30, 1958. Paul P. O'Brien, Clerk.

No. [illegible]

[illegible] States Court of Appeals

[illegible]

[illegible] Day of Federal Savings and Loan Association [illegible], Los Angeles, California,

Appellant,

vs.

[illegible] Gutierrez,

Appellee.

[illegible]PPELLANT'S OPENING BRIEF.

[illegible] W. Wenig,
[illegible] States Attorney,
[illegible] C. Lavine,
[illegible] U. S. Attorney,
[illegible] of Civil Division,
[illegible] Thomson,
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FILED

[illegible] 1958

PAUL P. O'BRIEN, CLERK

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No. 16105

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

RICHARD C. HOY, as District Director of the Immigration and Naturalization Service, Los Angeles, California,

Appellant,

vs.

ARNULFO ROJAS-GUTIERREZ,

Appellee.

APPELLANT'S OPENING BRIEF.

Jurisdiction.

Appellee, plaintiff below, brought an action in the District Court seeking judicial review of an order of deportation [R. 3-8].[1] Jurisdiction there was invoked pursuant to 28 U. S. C. 2201 (the Declaratory Judgment Act) and 5 U. S. C. 1009 (Section 10 of the Administrative Procedures Act).

Since the judgment of the District Court [R. 26-27] was a final decision, this Honorable Court has jurisdiction of an appeal from that decision pursuant to 28 U. S. C. Secs. 1291 and 1294(1).

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[1]"R." refers to the printed Transcript of Record.

Statement of the Case.

On December 2, 1957, appellee filed a "Petition for Judicial Review and Declaratory Judgment: Injunction" [R. 3-8], seeking judicial review of an order of deportation. Plaintiff, an alien, alleged that on September 28, 1956, he was served with an order to show cause by the Immigration and Naturalization Service, requiring him to show cause as to why he should not be deported from the United States on the charge that he had been convicted of a violation of law relating to the illicit possession of narcotic drugs as provided in 8 U. S. C. 1251(a)(11) [R. 5]; that on October 19, 1956, after a hearing, he was ordered deported pursuant to the order to show cause [R. 5]; that by virtue of his unsuccessful appeal to the Board of Immigration Appeals [R. 5] he had exhausted his administrative remedies [R. 7], and finally, that the order of deportation erroneously applied Section 1251(a)(11), *supra,* in that it provided for the deportation of an alien convicted of possessing "narcotic drugs," when in fact the plaintiff had been convicted of possessing "marihuana" [R. 7]. Appellee's petition concluded that the order of deportation was illegal and prayed for judgment sustaining this contention, as well as for an injunction prohibiting appellant Hoy from deporting him pursuant to the order.

Appellant, on December 2, 1957, answered [R. 8-12] appellee's petition with a general denial.

The pre-trial order [R. 12-16] filed March 3, 1958, recited as facts, among others, that plaintiff had twice been convicted in the State of California courts for possessing marihuana in violation of Sections 11160 and 11500 of the Health and Safety Code of California [R. 14]; and

that on July 18, 1956, 8 U. S. C. 1251(a)(11) was amended to provide for the deportation of an alien who at any time had been convicted of violating any law or regulation relating "to the illicit possession of or traffic in narcotic drugs" [R. 14]. The pre-trial order reveals that there were no issues of fact [R. 15], but that among the issues of law[2] involved was whether 8 U. S. C. 1251(a)-(11), as amended, included marihuana within "narcotic drugs" in the phrase "illicit possession of or traffic in narcotic drugs. . . ."

The Honorable William C. Mathes, in a written opinion filed April 25, 1958 [R. 16-23], sustained contentions of appellee on the grounds that his brother judge, the Honorable Harry C. Westover, had previously decided the question [R. 20] adversely to appellant.[3] Thereafter, judgment [R. 26-27] was entered granting appellee the relief he requested, and on June 9, 1958, appellant filed its notice of appeal.

Statement of Points.

The District Court erred as a matter of law when it construed "narcotic drugs" as used in 8 U. S. C. 1251(a)-(11), as amended, in the phrase ". . . who at any time has been convicted of a violation of . . . any law or regulation relating to the illicit possession of . . . narcotic drugs" as not including "marihuana."

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[2]No discussion in this brief is made of appellee's other contentions of law below because they did not form the bases of the opinion below [R. 23] and hence, are irrelevant here.

[3]Judge Westover's decision in *Hoy v. Mendoza-Rivera* has been appealed to this Honorable Court (C. A. No. 16107). The Government's opening brief is due November 18, 1958.

Question Presented.

Is "marihuana" included within the "narcotic drugs" provision of Title 8 U. S. C. Sec. 1251(a)(1) which reads ". . . who at any time has been convicted of a violation of . . . any law or regulation relating to the illicit possession of . . . narcotic drugs . . ."?

Statutes Involved.

Title 8 U. S. C. 1251(a), insofar as pertinent, reads:

> "Any alien in the United States . . . shall, upon the order of the Attorney General, be deported who —" 66 Stat. 204; enacted June 27, 1952.

Title 8 U. S. C. 1251(a)(11) was amended by Section 301(b), Public Law 728, 70 Stat. 575, July 18, 1956, to read as follows:

> "(11) is, or hereafter at any time after entry has been, a narcotic drug addict, or who at any time has been convicted of a violation of, *or a conspiracy to violate,* any law or regulation relating to the illicit *possession of or* traffic in narcotic drugs, or who has been convicted of a violation of, *or a conspiracy to violate,* any law or regulation governing or controlling the taxing, manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation, exportation, or the possession for the purpose of manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation, or exportation of opium, coca leaves, heroin, marihuana, any salt derivative or preparation of opium or coca leaves or isonipecaine or any addiction-forming or addition-sustaining opiate;" [The italicized words are the words added by amendment in Public Law 728; otherwise the section reads as when it was enacted as part of 8 U. S. C. 1251(a) on June 27, 1952.]

ARGUMENT.

I.

Public Law 728 Clearly Shows That Congress Regarded "Marihuana" and "Narcotic Drugs" Violators to Be in Pari Delicto and Intended That the Statutes' Sanctions Be Applied Indiscriminately to Both Classes of Offenders.

Initially, it must be conceded, that nowhere in Public Law 728 does Congress expressly define "narcotic drugs" or "marihuana" and, indeed, even therein refers conjunctively to "narcotic drugs and marihuana." Thus, to cite a single example, Public Law 728 itself is described as an Act ". . . to provide for a more effective control of narcotic drugs and marihuana and for other related purposes." (70 Stat. 567.) Further, in substantive criminal statutes, Congress has definitionally differentiated between "narcotic drugs" (26 U. S. C. 4731) and "marihuana" (26 U. S. C. 4761). Yet, this is not a universal distinction. Thus, for civil purposes, in 42 U. S. C. 201(j) and 49 U. S. C. 787(d), Congress included "marihuana" (or "Indian hemp") in its definitions of "narcotics" or "narcotic drugs." However, in Title 8 U. S. C. (viz. Secs. 1182(a)(23) and 1251(a)(11)) Congress uses "narcotic drugs" and "marihuana" without expressly defining the terms.[4]

What was the purpose of Public Law 728, or "The Narcotic Control Act of 1956"?[5] Quite clearly it was prompted

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[4]It will be argued *infra* that the omission of the "narcotic drug" definition is both significant and deliberate. Congress, then, depending upon the intended purpose of particular legislation, may define "narcotic drugs" independently of "marihuana," as including "marihuana," or not at all.

[5]70 Stat. 567.

by a social problem Congress thought to be critical—the "narcotics problem."[6] If for Federal criminal statutes Congress has recognized a theoretical dissimilarity between "marihuana" and "narcotic drugs," Congress has surely shown that in terms of their practical social consequences it regards "marihuana" and "narcotic drugs" as Siamese twins. For it is together and not singly that these substances and their traffic constitute the "narcotics problem." Compare *Caudillo v. United States,* 253 F. 2d 513 (9 Cir., 1958). It is apparent from Public Law 728, 70 Stat. 567 *et seq.,* that Congress intended to deal equally with the marihuana and the narcotic drug offender.

That Congress regarded the marihuana and narcotic drug trafficker to be equally dangerous, and further intended that the same consequences befall them both, is nowhere better illustrated than in the penalty provisions of Federal Criminal Statutes relating to marihuana (*e.g.,* 21 U. S. C. 176(a)) or narcotic drugs (*e.g.,* 21 U. S. C. 174). With certain exceptions, sentences imposed for either violation are mandatory, 26 U. S. C. 7237; Sec. 103 Pub. Law 728, 70 Stat. 568. These penalty provisions, regardless of the substance dealt in, are equally severe.

It is certainly reasonable to conclude therefore, in face of this graphic display of legislative intent, that Congress desired to deport aliens convicted of "narcotics" violations, without any regard whatsoever to the identity of the substances involved, as another effective way of dealing with the "narcotics problem." To say that in 8 U. S. C.

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[6]". . . [The] illicit traffic in narcotic drugs and marihuana and their illegal uses" constitutes ". . . one of the most serious social problems confronting the American public today." H. R. 2388; 2 U. S. Cong. & Admin. News, 1956, at p. 3280.

1251(a)(11) Congress did not intend "marihuana" to be included within the meaning of ". . . illicit possession of . . . narcotic drugs" is to flout the congressional intent of the Narcotics Control Act of 1956. Such a construction by the barest of technicalities bestows an unintended and undesirable bonanza. Such a construction compels the absurd conclusion that Congress intended to smile upon the alien convicted of illegally possessing marihuana, and simultaneously to frown on the alien convicted of illegally possessing say, heroin. Clearly such an anomaly should be avoided. Congress, in Public Law 728, obviously desired to achieve broad social ends and the amending sections of Public Law 728 should therefore be broadly construed. Since Title 8 does not expressly define "narcotic drugs" it is submitted that Congress, to achieve its purpose, intended that "narcotic" be given its lay meaning: "A drug which in moderate doses allays sensibility, relieves pain, and produces profound sleep, but which in poisonous doses produces stupor, coma, or convulsions. Among the chief narcotics are "opium (with morphine), belladonna (with atropine), Indian hemp (*i.e.,* marihuana), strumonium and hyoscyasmis," *Webster's New International Dictionary,* 2d Ed. 1956.

II.

Congress Intended That the 8 U. S. C. 1251(a)(11) Phrase, "Possession of Narcotic Drugs," Incorporate State Criminal Statutes' Definition of "Narcotic Drugs."

Prior to his deportation hearing, appellee had been convicted of violating Section 11500 of the Health and Safety Code of California which provides, among other things, that ". . . no person shall possess . . . a narcotic [with inapplicable exceptions]." Section 11001 of that

same Code states that "narcotics . . . means any of the following . . . (h) all parts of the plant *Cannabis sativa L.* (commonly known as marihuana). . . ." While California is apparently not among the forty-four states and three territories that have enacted the Uniform Drug Act (see 9B Uniform Laws Annotated 729), it nevertheless has enacted the definition section of the Uniform Drug Act, 9B U. L. A. Sec. 1, at page 281. However, the point of this apparent digression is that if "narcotic drugs" in the Section 1251(a)(11) phrase "illicit possession of . . . narcotic drugs" depends on state statutes for its interpretations, the order of deportation is valid and the judgment below should be reversed.

The pertinent portion of Title 8, U. S. C. 1251(a)(11) relates to the deportation of an alien convicted of ". . . any law . . . relating to the illicit possession of . . . narcotic drugs." By the use of the word "any" Congress obviously meant state "law[s]" relating to the illicit possession of "narcotic drugs." Congress could not have meant federal criminal laws or statutes because there is no federal crime *per se* for the mere possession of either narcotic drugs or marihuana. If Congress, in Title 8, had expressly provided a definition of "narcotic drugs" that definition naturally would have controlled in applying state laws (*Nicholson v. United States,* 141 F. 2d 552 (9 Cir., 1944)). But, in absence of such an express federal definition, "narcotic drugs" must, if the words "possession of" are to be given meaning, refer to the applicable state laws. The reason Congress did not expressly define "narcotic drugs" in 8 U. S. C. 1251(a)(11), it is submitted, is that full effect could thereby be given to the various state statutory definitions thereof. (*United States v. Eramdjian,* 155 Fed. Supp. 914, 931 (S. D. Cal. 1957).)

Conclusion.

In conclusion, appellant respectfully submits to this Honorable Court:

1. That the whole import and purpose of Public Law 728, 70 Stat. 567, was to deal harshly and indiscriminately with both narcotic drugs and marihuana offenders, including the deportation of aliens so convicted either in state or federal courts; and
2. That in any event, the Narcotic Control Act's amendment of 8 U. S. C. 1251(a)(11) to read "illicit possession of . . . narcotic drugs" was designed to incorporate state statutory definitions of "narcotic drugs," including such definitions that incorporated "marihuana"; and

Hence, for either or both of these reasons the judgment appealed from below should be reversed.

Respectfully submitted,

LAUGHLIN E. WATERS,
United States Attorney,

RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,

HENRY P. JOHNSON,
Assistant U. S. Attorney,

Attorneys for Appellant.

No. 16106

United States Court of Appeals

for the Ninth Circuit

UNITED STATES OF AMERICA,

Appellant.

vs.

HERBERT D. HOVER, Doing Business as Ciro's,

Appellee.

Transcript of Record

Appeal from the United States District Court for the Southern District of California Central Division

FILE
DEC 17 1958
PAUL P. O'BRIEN, C

Phillips & Van Orden Co., 4th & Berry, San Francisco, Calif.—12-5-58

No. 16106

United States Court of Appeals for the Ninth Circuit

UNITED STATES OF AMERICA,

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Phillips & Van Orden Co., 4th & Berry, San Francisco, Calif.—12-5-58

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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For Appellee:

ERNEST R. MORTENSON,
961 E. Green Street,
Pasadena, California.

In the District Court of the United States for the Southern District of California, Central Division

No. 20853-WM

HERBERT D. HOVER, dba CIRO'S,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

COMPLAINT FOR RECOVERY OF TAXES

Comes now the plaintiff and complains of the defendent as follows:

1.

This is an action for recovery of cabaret taxes paid by the plaintiff pursuant to an assessment entered against the plaintiff on or about November 14, 1955. Said assessment was made under Sections 1700(e) of the Internal Revenue Code of 1939 and 4231(6) and 4232(b) of the Internal Revenue Code of 1954. Jurisdiction thereof is vested in this Court by 28 U.S.C. 1340; 1346(a)(1).

2.

At all times herein mentioned, plaintiff was and now is a citizen and a resident of the County of Los Angeles in the Southern District of California. [2*]

*Page numbering appearing at foot of page of original Certified Transcript of Record.

3.

During the periods June, 1951, through March 31, 1955, Plaintiff owned and operated a restaurant and night club under the name of Ciro's at 8433 Sunset Boulevard, Los Angeles 46, California.

4.

During the period specified in Number 3 above, Plaintiff paid cabaret tax assessments in the total amount of Four Hundred Forty Thousand, Four Hundred Seventy-one Dollars and Thirty-eight Cents ($440,471.38).

5.

On or about November 14, 1955, assessments over and above the Four Hundred Forty Thousand Four Hundred Seventy-one Dollars and Thirty-eight Cents ($440,471.38) cabaret tax paid for said taxable periods were made by the District Director of Internal Revenue in the total amount of Sixty-seven Thousand Six Hundred Sixty Dollars and Sixty-two Cents ($67,660.62).

6.

Said assessment of additional tax in the amount of Sixty-Seven Thousand, Six Hundred Sixty Dollars and Sixty-two Cents ($67,660.62) is based upon a Revenue Agent's Report dated September 29, 1955, in which is contained an analysis of purported additional taxable sales.

7.

In said Revenue Agent's Report additional taxable sales for the "Pavillion Room" were computed

as Three Hundred Thirty-three Thousand Four Hundred Ninety-one Dollars and Eighty-six Cents ($333,491.86); purported additional taxable sales for the "Ciroette Room" were computed to be Nine Thousand One Hundred Seventeen Dollars and Twelve Cents ($9,117.12) and additional taxable sales for "Closed House" parties were computed to be Fifty-seven Thousand Four Hundred Two Dollars and Fifty Centy [3] ($57,402.50).

8.

During the taxable periods involved, plaintiff owned and operated, separate from the main dining room, a room known as the "Pavillion Room."

9.

The "Pavillion Room" is on a different level and in a different building from Ciro's main room.

10.

When a separation wall installed between the "Pavillion Room" and the main dining room was closed, the customers in the "Pavillion Room" could not see or hear entertainment in the main room.

11.

During the periods herein involved, private parties were held in the "Pavillion Room" and the separation wall was closed between the two said rooms until after the groups in the "Pavillion Room" had concluded their private parties.

12.

Some guests at the private parties in the "Pavillion Room" remained in the "Pavillion Room" after the private party had been concluded.

13.

On some occasions the separation wall was opened between the "Pavillion Room" and the main room after conclusion of the private parties in the "Pavillion Room" so that patrons could view from that room, the floor show in the main room.

14.

At no time while members of the private parties in the "Pavillion Room" were viewing entertainment in the main room, did such members cease to be members of private parties. [4]

15.

At no time were the private parties held in the "Pavillion Room" open to the public.

16.

Rest Room accommodations for patrons in the "Pavilion Room" during the period here involved, were separate from the Rest Room accommodations for the main room.

17.

The hours of service and the wage scale are different for waiters serving in the "Pavillion Room" and in the main room and waiters serving in the

"Pavillion Room" usually finished between 8:00 p.m. and 9:00 p.m. but in no event stayed after 10:00 p.m.

18.

The "Pavillion Room" has a separate entrance from the main room.

19.

The parking lot arrangements are different for the patrons of the "Pavillion Room" and the main room.

20.

There is a difference in menus for the meals served in the "Pavillion Room" and in the main room.

21.

Under union rules, waiters in the "Pavillion Room" were permitted to serve no more than twenty (20) patrons, whereas waiters in the main room were permitted to serve an unlimited number of patrons.

22.

Members of private parties held in the "Pavillion Room" were charged different from patrons who were served in the main room.

23.

The examining officers determined that 94% of the "Pavillion Room" receipts were subject to cabaret tax. [5]

24.

A cabaret tax of 20/120% was applied to the purported additional taxable sales stated in Paragraph 23 above which tax totaled Fifty-five Thousand Five Hundred Eighty-one Dollars and Ninety-six Cents ($55,581.96).

25.

In determining the taxability of sales in the "Pavillion Room" the examining officers found as follows:

"The Pavillion Room is adjacent to the main dining room and capable of being separated from the main room by a sliding, accordion-like wall. When the sliding wall is drawn back, patrons in the Pavillion Room can view the entertainment which is presented in the main room. Private parties are frequently held in this room and at the time the entertainment commences in the main room, the sliding wall is retracted so that these private groups view the same show that is presented for patrons in the main room."

26.

Cabaret tax was neither collected from, nor passed on to organizations or members of private parties who were served in the "Pavillion Room."

27.

Plaintiff owned and operated a room called the "Ciroette Room" on the second floor of Ciro's.

28.

Patrons served in the "Ciroette Room" could observe or participate in the entertainment in the main room only by going down a flight of stairs and passing through at least two doorways.

29.

The "Ciroette Room" has separate Rest Room accommodations.

30.

In determining the taxability of sales in the "Ciroette Room" the examining officers concluded that 5% of the "Ciroette Room" receipts were subject to cabaret tax and computed such tax [6] to be a total of One Thousand Five Hundred Nineteen Dollars and Fifty-two Cents ($1,519.52).

31.

Plaintiff neither collected from nor passed on to customers in the "Ciroette Room" the cabaret tax assessed against him for charges, sales or service in the "Ciroette Room."

32.

The examining officers determined that receipts in the amount of Fifty-seven Thousand, Four Hundred Two Dollars and Fifty Cents ($57,402.50) from private parties, hereinafter called "Closed House" parties, held from time to time at Ciro's, were subject to cabaret tax.

33.

The amount of cabaret tax computed on "Closed House" private parties was Nine Thousand Five

Hundred Sixty-seven Dollars and Eight Cents ($9,567.08).

34.

"Closed House" private parties were conducted by various organizations which charged members specified prices which were paid to the organizations by the members.

35.

When "Closed House" parties were held, Ciro's was closed to the public.

36.

In some instances the organizations conducting the "Closed House" parties used the same entertainment as that currently appearing at Ciro's at the time the party was given and in other instances, such organizations provided their own entertainment.

37.

The examining officers in determining that "Closed House" parties were subject to cabaret tax deemed such parties to be the [7] same as the reservation of one or two tables at Ciro's.

38.

In nearly all instances, the private organizations conducting "Closed House" parties paid for the entertainment directly to the entertainers themselves.

39.

In nearly all instances, the private organizations conducting the "Closed House" parties made payment for dinner and beverages directly to plaintiff.

40.

Ciro's had, during the period here involved, separate checking facilities for the "Ciroette Room," "Pavillion Room" and the main room.

41.

On information and belief, hotels, restaurants and night clubs locally and nationally, generally have not in the past collected, and do not now collect, cabaret tax on services and sales such as those on which assessment was made herein.

42.

Defendant's agents, upon various audits of plaintiff's cabaret tax returns, deemed "Pavillion Room," "Ciroette Room" and "Closed House" party sales not to be subject to cabaret tax.

43.

In no instance was cabaret tax collected from or passed on to organizations conducting "Closed House" parties nor to the patrons thereof.

44.

The schedule attached hereto as Exhibit "A" and made a part hereof shows the amount of additional tax assessed for the various taxable periods from June, 1951, to the first quarter of 1955, inclusive. [8]

45.

On or about August 2, 1956, plaintiff paid Three Hundred Dollars ($300.00) on the above assessment.

46.

On or about August 2, 1956, a Claim for Refund in the amount of Three Hundred Dollars ($300.00) was filed by plaintiff, and on or about September 20, 1956, an amended claim was filed to correct a typographical error. Copies of said claim and amended claim are attached hereto as Exhibit "B."

47.

On or about December 6, 1956, a Notice of Disallowance of Claim was received by plaintiff. Copy of said Disallowance of Claim is attached hereto as Exhibit "C."

48.

Assessments made for the taxable periods ended more than four (4) years prior to the date of assessment herein, are invalid because of the prohibition of such assessment by Section 3312(a) of the Internal Revenue Code of 1949.

49.

Defendant has, at all times, failed or refused to refund the aforesaid cabaret taxes in the amount of Three Hundred Dollars ($300.00).

50.

By virtue of the foregoing, the United States became and is now indebted to the plaintiff in the amount of Three Hundred Dollars ($300.00) with interest as provided by law.

Wherefore, plaintiff claims judgment against the defendant in the amount of Three Hundred Dollars ($300.00) with interest thereon as provided by law.

/s/ ERNEST R. MORTENSON,
Attorney for Plaintiff. [9]

EXHIBIT A

(Copy)

Name and Address of Taxpayer:

Herbert D. Hover dba Ciro's
8433 Sunset Blvd.
Los Angeles 46, California

Date of Report: 9-29-55

Examining Officers: B. J. O'Connor
Chester M. Ross

Statement of Excise Tax Liability by Months

Month and Year		Correct Liability	Previously Assessed	Additional Tax Overassessment Interest
6-51	Tax Pen.	$ 6,259.86	$ 6,223.40	$ 36.46
7-51	Tax Pen.	12,010.39	11,993.20	17.19
8-51	Tax Pen.	6,160.61	6,133.55	27.06
9-51	Tax Pen.	10,150.23	10,124.28	25.95
10-51	Tax Pen.	8,938.38	8,892.40	45.98
11-51	Tax Pen.	9,698.07	9,661.80	36.27
12-51	Tax Pen.	8,777.77	8,701.80	75.97
1-52	Tax Pen.	9,202.23	8,586.60	615.63
2-52	Tax Pen.	8,503.61	7,802.40	701.21
3-52	Tax Pen.	9,222.04	8,766.60	455.44

Statement of Excise Tax Liability by Months

Month and Year		Correct Liability	Previously Assessed	Additional Tax Overassessment Interest
4-52	Tax Pen.	$ 8,248.02	$ 7,054.40	$ 1,193.62
5-52	Tax Pen.	15,008.10	13,393.80	1,614.30
6-52	Tax Pen.	11,284.41	8,615.20	2,669.21
7-52	Tax Pen.	8,722.63	7,999.91	722.72
8-52	Tax Pen.	9,425.93	8,800.20	625.73
9-52	Tax Pen.	11,625.67	9,972.00	1,653.67
10-52	Tax Pen.	17,521.62	16,239.80	1,281.82
11-52	Tax Pen.	9,040.93	5,752.79	3,288.14
12-52	Tax Pen.	11,124.05	8,069.40	3,054.65
1-53	Tax Pen.	14,523.05	12,712.00	1,811.05
2-53	Tax Pen.	10,143.94	8.015.20	2,128.74
3-53	Tax Pen.	11,599.70	9,624.17	1,975.53
4-53	Tax Pen.	12,808.50	11,257.80	1,550.70
5-53	Tax Pen.	14,093.66	11,930.65	2,163.01
6-53	Tax Pen.	11,164.71	9,321.62	1,843.09
3-53	Tax Pen.	30,935.52	28,424.38	2,511.14
4-53	Tax Pen.	35,067.49	26,995.32	8,072.17
1-54	Tax Pen.	33,053.63	27,510.99	5,542.64
2-54	Tax Pen.	30,835.16	25,577.08	5,258.08
3-54	Tax Pen.	36,853.95	34,270.82	2,583.13
4-54	Tax Pen.	31,993.74	24,683.52	7,310.22
1-55	Tax Pen.	44,134.40	37,364.30	6,770.10
		$508,132.00	$440,471.38	$ 67,660.62

EXHIBIT B

Form 843

U. S. Treasury Department,
Internal Revenue Service

Claim

Kind of claim filed:

Refund of Taxes Illegally, Erroneously, or Excessively Collected.

Name of taxpayer or purchaser of stamps:

Herbert D. Hover, d/b/a Ciro's.

Number and street:

8433 Sunset Boulevard.

City, town, postal zone, State:

Los Angeles 46, California.

1. District in which return was filed:

Los Angeles.

2. Name and address shown on return, if different from above:

Same.

3. Period—If for tax reported on annual basis, prepare separate form for each taxable year:

From April 1, 1951*, to April 30, 1951*.

4. Kind of tax:

Cabaret.

5. Amount of assessment:
$1,193.62.

Dates of payment:
August 2, 1956.

* * *

7. Amount to be refunded:
$300.00.

* * *

9. The claimant believes that this claim should be allowed for the following reasons:

See Rider Attached Hereto and Made a Part Hereof

[*Corrected to read 1952 on original—see Amended Claim, page 19 of printed record.]

I declare under the penalties of perjury that this claim (including any accompanying schedules and statements) has been examined by me and to the best of my knowledge and belief is true and correct.

Dated: August 2, 1956.

/s/ HERBERT D. HOVER,
d/b/a Ciro's;

By /s/ ERNEST R. MORTENSON,
Attorneys in Fact. [12]

Instructions

* * *

Herbert D. Hover, d/b/a Ciro's
Rider Attached to Form 720

A "Monthly Amended Federal Excise Tax Return" (Form 720) was filed by mail August 2, 1956, by taxpayer in which tax was reported as follows:

"Examining officers, B. J. O'Conner and Chester M. Ross, in a report dated September 29, 1955, computed additional tax due for the month of April, 1952, as follows:

Cabaret Tax Reported Taxable Sales Tax Included	Additional Taxable Sales Pavillion Room	Additional Taxable Sales Ciroette Room	Additional Taxable Sales "Closed House" Parties
$42,362.40	$ 5,017.49	$ 194.13	$ 1,950.10

Corrected Taxable Sales Tax Included	Cabaret Tax Due $\frac{20 \text{ x Col. } 6}{120}$	Total Tax Due
$49,488.12	$ 8,248.02	$ 8,248.02

On taxpayer's original tax return for the month of April, 1952, the tax assessed was $7,054.40, therefore according to the examining officers' report, there is an additional tax due and owing of $1,193.62. Taxpayer does not believe he is subject to any additional cabaret tax. He considers the interpretation to be erroneous under which the additional deficiency has been determined.

Accordingly, this return is being filed without conceding the validity of the rulings, interpretations or computations relied upon by the District Director of Internal Revenue.

Taxpayer paid to the District Director of Internal Revenue three hundred dollars ($300.00) at the time of filing said return.

Taxpayer asserts as grounds for this claim that he did not maintain in the Ciroette Room, nor for so-called "Closed House" parties any roof garden, cabaret, or similar place furnishing a public performance for profit, by or for any patron or guest within the meaning of Section 1700(e) of the 1939 Code or Sections 4231 (6) and 4233 (b) of the 1954 Code. [13]

Taxpayer contends that the tax was imposed on persons who neither witnessed nor were present at any taxable entertainment.

The tax was erroneously assessed on charges for service and refreshment to persons who were not patrons or guests admitted to a place furnishing a public performance for profit.

In addition to his contention that there is no factual basis for the assessment, taxpayer asserts that the regulations and rulings under which the cabaret tax was assessed on charges in the Pavillion Room, the Ciroette Room and on "Closed House" parties are an erroneous interpretation of Section 1700(e) of the 1939 Code, are in conflict with Court decisions and are invalid.

U. S. Treasury Department,
Internal Revenue Service

Form 843

Amended Claim

Kind of claim filed:
Refund of Taxes Illegally, Erroneously, or Excessively Collected.

Name of taxpayer or purchaser of stamps:
Herbert D. Hover, d/b/a Ciro's.

Number and street:
8433 Sunset Boulevard.

City, town, postal zone, State:
Los Angeles 46, California.

1. District in which return was filed:
Los Angeles.

2. Name and address shown on return, if different from above:
Same.

3. Period:
From April 1, 1952, to April 30, 1952.

4. Kind of tax:
Cabaret.

5. Amount of assessment:
$1,193.62.

Dates of payment:
August 2, 1956.

* * *

7. Amount to be refunded:
$300.00.

* * *

9. The claimant believes that this claim should be allowed for the following reasons:

(This Amended claim is filed to correct a typographical error in the original dated August 2, 1956. The original claim under Item No. 3 gives the period as "April 1, 1951, to April 30, 1951." This has been corrected as shown above.)

I declare under the penalties of perjury that this claim (including any accompanying schedules and statements) has been examined by me and to the best of my knowledge and belief is true and correct.

Dated: September 20, 1956.

/s/ HERBERT D. HOVER,
d/b/a Ciro's;

By /s ERNEST R. MORTENSON,
Attorney in Fact. [15]

Instructions

* * *

EXHIBIT C

U. S. Treasury Department
Internal Revenue Service
District Director
Los Angeles 12, Calif.

December 5, 1956.

Mr. Herbert D. Hover,
d/b/a Ciro's.
c/o Ernest R. Mortenson,
3826 East Colorado,
Pasadena 8, California.

Claim for Refund of $300.00.
Taxable Period: 4/1/52 to 4/30/56.

In accordance with the provisions of Section 3772 (a) (2) of the Internal Revenue Code, this notice of disallowance in full of your claim or claims is hereby given by registered mail.

By direction of the Commissioner:

Very truly yours,

/s/ R. A. RIDDELL,
District Director.

Registered Mail 154740.

Duly verified.

[Endorsed]: Filed December 21, 1956. [16]

[Title of District Court and Cause.]

AMENDED ANSWER AND COUNTERCLAIM FOR COLLECTION OF CABARET TAXES

Comes Now the defendant, United States of America, and pursuant to stipulation and order of June 21, 1957, files this, its amended answer to plaintiff's complaint and counterclaim for collection of cabaret taxes, and admits, denies and alleges as follows:

Amended Answer

1.

Admits the allegations of the first two sentences of paragraph 1. Denies that jurisdiction of this action is vested in this Court.

2.

Admits the allegations of paragraph 2. [30]

3.

Admits the allegations of paragraph 3.

4.

Admits the allegations of paragraph 4.

5.

Admits the allegations of paragraph 5.

6.

Admits the allegations of paragraph 6, but it is denied that the sales were not taxable.

7.

Admits the allegations of paragraph 7, but it is denied that any of the sales were not taxable.

8.

Admits the allegations of paragraph 8, but it is denied that the "Pavillion Room" was "separate from the main dining room" or was operated "separate from the main dining room."

9.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 9 of the complaint.

10.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 10 of the complaint.

11.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 11 of the complaint.

12.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 12 of the complaint. [31]

13.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 13 of the complaint.

14.

Denies the allegations of paragraph 14.

15.

Denies the allegations of paragraph 15.

16.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 16 of the complaint.

17.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 17 of the complaint.

18.

Denies the allegations of paragraph 18.

19.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 19 of the complaint.

20.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 20 of the complaint.

21.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 21 of the complaint.

22.

Denies the allegations of paragraph 22. [32]

23.

Admits the allegations of paragraph 23.

24.

Admits the allegations of paragraph 24, but it is denied that the sales were not taxable.

25.

Admits the allegations of paragraph 25, but it is denied that the alleged findings were the only findings upon which the taxability of the sales was determined.

26.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 26 of the complaint.

27.

Admits the allegations of paragraph 27.

28.

Admits the allegations of paragraph 28.

29.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 29 of the complaint.

30.

Admits the allegations of paragraph 30.

31.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 31 of the complaint.

32.

Admits the allegations of paragraph 32, except denies the parties were private.

33.

Admits the allegations of paragraph 33, except denies [33] the parties were private.

34.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 34 of the complaint.

35.

Denies the allegations of paragraph 35.

36.

Admits the allegations of paragraph 36, but denies the allegation that the organizations referred to provided their own entertainment.

37.

Admits the allegations of paragraph 37.

38.

Denies the allegations of paragraph 38.

39.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 39 of the complaint.

40.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 40 of the complaint.

41.

Denies the allegations of paragraph 41.

42.

Denies the allegations of paragraph 42.

43.

Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 43 of the complaint. [34]

44.

Admits the allegations of paragraph 44.

45.

Admits the allegations of paragraph 45.

46.

Admits the allegations of paragraph 46.

47.

Admits the allegations of paragraph 47.

48.

Denies the allegations of paragraph 48.

49.

Admits the allegations of paragraph 49.

50.

Denies the allegations of paragraph 50.

Counterclaim

For a Counterclaim to Plaintiff's Complaint Herein, Defendant Alleges as Follows:

1.

On November 14, 1955, the authorized delegate of the Secretary of the Treasury assessed against the plaintiff, Herbert D. Hover, d/b/a Ciro's, cabaret taxes for the monthly periods June 1, 1951, through June 30, 1953, and for the quarterly periods July 1, 1953, through March 31, 1955, in the sum of $67,660.62 taxes and $7,858.51 interest, for a total assessment of $75,519.13; notice of the assessment of said tax and interest was given to the plaintiff and demand for the payment thereof was made upon him on November 16, 1955; on August 7, 1956, the sum of $300.00, and no more, was paid; with respect to said assessment there remains due, owing and unpaid to the United States of America the balance of the assessment in the sum of $75,219.13, together with accrued interest thereon according to law, which amounted to [35] the sum of $6,599.44 on June 30, 1957, and which continues to accrue at the statutory rate of six per centum per annum, or $12.36 per day, thereafter.

2.

The taxes assessed against the plaintiff as alleged in paragraph 1 were equivalent to 20% of all the amounts paid during said periods for admission, refreshment, service or merchandise to plaintiff by or for any patron or guest of the plaintiff's establishment in the portions of plaintiff's establishment referred to as the Pavillion Room and Ciroette Room, and for the entire establishment on those occasions in which the facilities of the establishment were made available to one organization exclusively.

3.

Throughout said period plaintiff furnished to the said patrons or guests of the facilities set forth in paragraph 2 herein, by or for whom the said payments were made, public performances for profit such as dancing to orchestral music, singing, comedy entertainment, as well as other varied types of entertainment.

4.

Plaintiff, by reason of the aforesaid assessment, is indebted to the defendant in the sum of $81,-819.07 together with interest at the rate of $12.36 per day from July 1, 1957, until paid, and defendant is entitled to judgment against the plaintiff for said amount.

Wherefore, defendant prays for judgment as follows:

(1) That the complaint be dismissed with prejudice and it be adjudged and decreed that plaintiff take nothing from the defendant;

(2) That defendant have judgment against [36] plaintiff for the sum of $81,819.07, together with interest at the rate of $12.36 per day from July 1, 1957, until paid; and

(3) That defendant have its costs and disbursements of this action.

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant United States Attorney, Chief, Tax Division;

/s/ EDWARD R. McHALE,
Attorneys for Defendant,
United States of America.

Affidavit of Service by Mail attached.

[Endorsed]: Filed September 4, 1957. [37]

[Title of District Court and Cause.]

REPLY TO COUNTERCLAIM

Plaintiff, for reply to the counterclaim of the defendant set forth in paragraphs 1 to 4 of the Answer filed herein, says:

1.

Replying to paragraph 1 of said counterclaim, plaintiff admits the allegations therein except that plaintiff denies that there remains due, owing and unpaid to the United States of America the balance

of the assessment in the sum of Seventy-five thousand Two Hundred Nineteen Dollars and Thirteen Cents ($75,219.13) together with accrued interest.

2.

Replying to paragraph 2 of said counterclaim, plaintiff admits that the assessment was computed on the basis of 20% of certain amounts paid during said periods for admission, refreshment service or merchandise, but denies that plaintiff's [55] establishment was subject to the tax assessed.

3.

Replying to paragraph 3 of said counterclaim, plaintiff denies the allegations therein.

4.

Replying to paragraph 4 of said counterclaim, plaintiff denies the allegations therein.

Wherefore, plaintiff demands that defendant's counterclaim be dismissed and that he be awarded judgment as prayed in the Complaint.

/s/ ERNEST R. MORTENSON,
Attorney for Plaintiff.

Dated: 9th day of Sept., 1957.

Receipt of copy acknowledged.

[Endorsed]: Filed September 10, 1957. [56]

[Title of District Court and Cause.]

GOVERNMENT'S ANALYSIS OF STIPULATION JOINT EXHIBIT 2-B

Joint Exhibit 2-B to the stipulation is a concise summary of taxpayer's records of 304 banquets held in the Pavillion Room during the period involved.

For the convenience of the Court, defendant has analyzed the comments appearing in the contracts for the various parties and has summarized them. The following is a summary of the number of times the various comments appear in the comment column of said exhibit:

Code-Comment Column	No. of Times Appearing
A. None	3
B. No dance floor or music piped in	0
C. Provide own show	1
D. All women	1
E. All men	18
F. Music from main room piped in	17
G. Music from main room piped in for dancing	253
H. Orchestral music piped in	6
I. See show	37
J. I'll inform you what show will appear	1
K. At show time accordion wall folds back for party to see show	4
L. Move to main entertainment room without charge	1
M. No dancing	18
N. Dancing	5

O. Additional charge of $1.00 conditioned on presence of Sophie Tucker or similar entertainment 0
P. Some of guests play cards after dinner..... 4
Q. $1.00 per person cover for reservation for main room to see first show..... 0
R. Own orchestra 1
S. Tax after entertainment starts..... 2
T. Business until show time, then see show... 2
U. Stay until closing of Ciro's..... 0
V. Bar open until closing of Ciro's.....125
W. Bridge tables 1
X. .....; Time at which drink price to be raised (10:00) 4
(10:30) 3
Y. Drink price raised at show time.....257
Z. If room, will see show..... 0
AA. See first show..... 11
BB. See second show..... 2
CC. Piano in Pavillion Room..... 1

The material and pertinent facts appearing from said summary are as follows: [83]

(1) That for almost all of the parties it was contemplated between Ciro's and the persons arranging the parties that the group would see the floor show. For instance, there are 37 specific comments, I, "See show"; there is 1 specific comment, J, "I'll inform you what show will appear"; there are 4 comments, K, "At show time accordion wall folds back for party to see show"; there is 1 comment, L, "Move to main entertainment room with-

out charge"; there are 2 comments, S, "Tax after entertainment starts"; there are 2 comments, T, "Business until show time, then see show"; there are 11 comments, AA, "See first show"; there are 2 comments, BB, "See second show"; there are 7 comments, X, ".....; Time at which drink price to be raised"; and there are 257 comments, Y, "Drink price raised at show time." In all, these contractual arrangements indicating that the groups would see the show, total 314.

(2) On the other hand, there is but one comment, C, "Provide own show," from which it can be reasonably inferred that the group did not participate or witness the entertainment. There are one or two other occasions on which it possibly could be inferred that the group did not witness the entertainment, such as, A, in which there was no comment on three occasions; R, "Own orchestra" on one occasion; and, possibly, P, "Some of guests play cards after dinner," on four occasions; and W, "Bridge tables" on one occasion. However, it will be noted that the assessment is based only on 96% of the receipts of the Pavillion Room, and the small number in which it might reasonably be inferred that the guests did not witness the floor show would not represent more than 4% of the gross receipts.

(3) There is one matter of particular significance the Government wishes to call to the Court's attention. There are 257 occasions on which the drink price was raised from 75 cents at dinner time

to 90 cents at show time. This is an increase of 20%. The federal cabaret tax was 20%. However, the evidence will show that no part of this 20% increase in price of the alcoholic beverages [84] sold to the patrons of the Pavillion Room was paid over to the Federal Government as cabaret taxes.

Respectfully submitted,

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant United States Attorney, Chief, Tax Division;

/s/ EDWARD R. McHALE,
Attorneys for Defendant,
United States of America.

[Endorsed]: Filed December 19, 1957. [85]

[Title of District Court and Cause.]

STIPULATION RE COMPUTATION

Pursuant to the request of the Court that the parties agree in advance on computations in the event of a court decision on one theory of the case,

It Is Hereby Stipulated by and between the parties hereto through their respective counsel of record, with respect to the Pavillion Room, subject to

the objections of materiality and relevancy, as follows:

1. That the serving of food was completed in every instance prior to 10:30 p.m.

2. That plaintiff does not have retained records showing either the time when cash sales of refreshments were made or what proportion of drinks were sold before and after the drink price was advanced from 75c to 90c, for the evenings involved. [86]

3. For the purposes of this stipulation, the parties have agreed in the event it becomes necessary for this Court's judgment, based on the facts known to the parties set forth in the evidence, e.g., as to the duration of the parties, that two-thirds of the refreshments were served to the patrons of the Pavillion Room before show time of 10:30 p.m. and one-third thereafter.

4. That this stipulation is not a stipulation as to the time when payments were made for either food or refreshments.

5. Based on the foregoing paragraphs, it is stipulated if it becomes necessary for the Court's decision, taking into consideration that 6% of the amounts paid for admissions, refreshments, service or merchandise were not treated as taxable, that with respect to the $55,581.98 tax assessed [Plaintiff's Exhibit 1], $39,980.08 would represent tax on food served, $5,200.63 would represent tax on beverages served after 10:30 p.m., and $10,401.27 would represent tax on beverages served prior to 10:30 p.m.

Dated: December 23, 1957.

/s/ ERNEST R. MORTENSON,
Attorney for Plaintiff.

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant United States Attorney, Chief, Tax Division;

/s/ EDWARD R. McHALE,
Attorneys for Defendant.

[Endorsed]: Filed December 26, 1957. [87]

[Title of District Court and Cause.]

MINUTES OF THE COURT, DEC. 19, 1957

At: Los Angeles, Calif.

Present: Hon. Irving Kaufman, District Judge.
Counsel for Plaintiff Ernest R. Mortenson.
Counsel for Defendant: Edward R. McHale, Assistant U. S. Attorney.

Proceedings:

For Court trial. Court convenes at 10:12 a.m. Council for both sides answer ready. Court orders trial proceed.

Counsel for plaintiff makes opening statement.
Attorney for Gov't makes opening statement.
Court declares a recess at 11:00 a.m. Court recon-

venes at 11:07 a.m. Counsel for both sides answer ready. Court orders trial proceed.

Plf's Ex. 1, 2, 3-A, 3-B, 3-C, 3-D, 4-A, 4-B, and 4-C, heretofore marked for ident., are now admitted in evidence.

Plf's Ex. 5 is marked for ident. and admitted in evidence.

Herbert D. Hover is called, sworn, and testifies in his own behalf as plaintiff.

Plf's Ex. 6 is marked for ident. and admitted in evidence.

Plf's Ex. 7 is marked for ident. and admitted in evidence.

Court declares a recess at 12:05 p.m.

Filed Government's analysis of stipulated joint exhibit.

Court reconvenes at 2:00 p.m. Counsel for both sides answer ready. Court orders trial proceed.

Attorney Mortenson makes explanatory statement.

Witness Hover, heretofore sworn, resumes the stand and testifies further.

Plf's Ex. 8 is marked for ident. only.

Plf's Ex. 6-A is marked for ident. and admitted in evidence.

Court, counsel, and witness confer on Exhibit 8.

Court declares a recess at 2:40 p.m. to reconvene at Ciro's.

Filed plaintiff's supplemental memo. of law.

Court reconvenes at 3:30 p.m. at Ciro's for inspection of premises. Counsel for both sides, Wit-

ness Hover, reporter, and deputy clerk are present. Court orders conference re inspection to proceed.

At 4:00 p.m. It Is Ordered that cause is continued to Dec. 20, 1957, 10:00 a.m., for further Court trial. Court adjourns.

JOHN A. CHILDRESS,
Clerk;

By /s/ IRWIN YOUNG,
Deputy Clerk. [96]

[Title of District Court and Cause.]

MINUTES OF THE COURT, DEC. 20, 1957

Present: Hon. Irving R. Kaufman, District Judge.
Counsel for Plaintiff: Ernest R. Mortenson.
Counsel for Defendant: Edward R. McHale, Assistant U. S. Attorney.

Proceedings:

For further Court trial. Court convenes at 10:05 a.m. Counsel for both sides answer ready. Court orders trial proceed.

Witness Hover, heretofore sworn, resumes the stand and testifies on cross-examination.

Deft's Ex. A is marked for ident. and admitted in evidence.

Vincent Johnson is called, sworn, and testifies on behalf of defendant.

Deft's Ex. B is marked for ident. and admitted in evidence.

Court recesses at 10:55 a.m. Court reconvenes at 11:10 a.m. Counsel for both sides answer ready. Court orders trial proceed.

Frederick C. Payne is called, sworn, and testifies on behalf of defendant.

Deft's Ex. C is marked for ident. only.

Court and counsel argue.

Witness Francis V. McGinley is called, sworn, and testifies on behalf of defendant.

Deft's D is marked for ident.

Deft's Ex. E is marked for ident. and admitted in evidence.

James R. Westengard is called, sworn, and testifies on behalf of defendant.

Court and counsel confer on possible stipulation to eliminate necessity of calling certain witnesses following a substantially similar line of testimony.

Deft's Ex. F is marked for ident. and admitted in evidence.

Court recesses at 11:55 a.m.

Court reconvenes at 2:02 p.m. Counsel for both sides are present. Court orders trial proceed.

Filed stipulation (as Deft's Ex. G, which is marked for ident. and received in evidence) re testimony and excuse of witnesses pursuant to oral stipulation.

Marvin E. Stephens is called, sworn, and testifies on behalf of defendant.

Deft's Ex. H is marked for ident. and admitted in evidence.

Deft's Ex. H-1 is marked for ident. and admitted in evidence.

Witness Hover resumes the stand and testifies further.

Plaintiff rests.

Glen H. Harker is called, sworn, and testifies on behalf of defendant.

Raymond J. Schiever is called, sworn, and testifies on behalf of defendant.

At 2:35 p.m. court recesses. Court reconvenes at 3:15 p.m. Counsel for both sides are present. Court orders trial proceed.

Court makes a statement and counsel discuss preparation of stipulation re amount of tax, depending upon ruling of the Court.

Herman Kroll is called, sworn, and testifies on behalf of defendant.

Deft's Ex. I is marked for ident.

Dolores Miller is called, sworn, and testifies on behalf of defendant.

Deft's Ex. J-1 through J-9 are marked for ident. and admitted in evidence.

It Is Ordered that cause is continued to Dec. 23, 1957, 10:00 a.m., for further trial.

Court adjourns at 4:10 p.m.

JOHN A. CHILDRESS,
Clerk;

By /s/ IRWIN YOUNG,
Deputy Clerk. [97]

[Title of District Court and Cause.]

MINUTES OF THE COURT, DEC. 23, 1957

Present: Hon. Irving R. Kaufman, District Judge.
Counsel for Plaintiff Ernest R. Mortenson.
Counsel for Defendant: Edward R. McHale, Assistant U. S. Attorney.

Proceedings:

For further Court trial. Court convenes at 10:05 a.m. Counsel for both sides are present. Court orders trial proceed.

Warren Penn is called, sworn, and testifies on behalf of defendant.

Deft's Ex. K is marked for ident. and admitted in evidence.

Sol. Hirschhorn is called, sworn, and testifies on behalf of defendant.

Deft's Ex. L is marked for ident. and admitted in evidence.

David S. Greenberg is called, sworn, and testifies on behalf of defendant.

Deft's Ex. O and P are marked for ident. and admitted in evidence.

Counsel stipulate orally as to taxable "closed" houses.

Chester M. Ross is called, sworn, and testifies for defendant.

Gov't rests.

Plf's Ex. 9 is marked for ident.

It Is Ordered that cause is continued to 10:00 a.m., Dec. 26, 1957, for further Court trial.

Court adjourns at 10:50 a.m.

JOHN A. CHILDRESS,
Clerk;

By /s/ IRWIN YOUNG,
Deputy Clerk. [98]

[Title of District Court and Cause.]

MINUTES OF THE COURT, DEC. 26, 1957

Present: Hon. Irving R. Kaufman, District Judge.
Counsel for Plaintiff: Ernest R. Mortensen.
Counsel for Defendant: Edward R. McHale, Assistant U. S. Attorney.

Proceedings:

For further Court trial.

Court convenes at 10:02 a.m. Counsel for both sides answer ready. Court orders trial proceed.

Counsel discuss stipulation and It Is Ordered that stipulation re computation be filed.

Attorney Mortensen makes final argument.

Court recesses at 10:50 a.m. Court reconvenes at 11:00 a.m. Counsel for both sides answer ready. Court orders trial proceed.

Attorney McHale makes final argument.

Attorney Mortensen makes rebuttal argument.
Court makes a statement.

Court Orders that the cause stand submitted.

JOHN A. CHILDRESS,
Clerk;

By /s/ IRWIN YOUNG,
Deputy Clerk. [99]

[Title of District Court and Cause.]

OPINION

Irving R. Kaufman, D. J.

This suit was originally brought by plaintiff, proprietor of Ciro's, a nightclub, for refund of $300 paid pursuant to a deficiency of $67,660.62 in cabaret taxes assessed against him for the period between June 1, 1951 and March 31, 1955. Defendant has counterclaimed for $75,219.13, the unpaid balance of said assessment and interest.[1]

Ciro's, located on Sunset Boulevard in Los Angeles, is subdivided into three rooms in which the services and facilities of the Club are offered to the public. In addition to the main entertainment and dining room, hereinafter referred to as the "Main

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[1]Of the original assessment of $67,660.62, $992 by stipulation is conceded to be owing and not in issue in this suit.

Room," there are the "Pavillion" and "Ciroette" rooms. A lounge or cocktail bar located adjacent to the Main Room also serviced Ciro's patrons but its operations are not involved in this suit. In issue in this proceeding are the taxability of receipts from (1) the Pavillion Room, (2) the Ciroette Room and (3) the "closed house parties"—when the entire club was closed to the public and reserved for the exclusive use of private organizations. [101] In the interest of simplicity and organization, I shall discuss separately these three operations forming the basis of the tax.

Pavillion Room

The Pavillion Room is located adjacent to the lounge (which is basically a raised extension of the Main Room) and is separated therefrom by a movable wall and thick, soundproof curtain. It is undisputed that this room was used primarily to accommodate private organizations which desired to reserve for the evening such a room for the exclusive use of its members. The charges incurred or expended by these organizations or its members availing themselves of the facilities of the Pavillion Room form the basis of the cabaret tax assessment here in dispute. It is the Government's contention that the opportunity to witness the floor show in the Main Room was a strong inducement to these organizations to make their arrangements with Ciro's and that indeed, at the appropriate time the movable partition separating the Main Room and the Pavillion Room was opened so as to permit the

Pavillion Room guests to view the floor show in the Main Room. It follows, the Government argues, that such guests were entitled to be present during the furnishing of a public performance for [102] profit within the meaning of Int. Rev. Code of 1954, Section 4231(6),[2] and that the receipts obtained in the Pavillion Room both before and after the separation was removed are subject to the cabaret tax. More specifically, the Government is here seeking to sustain a cabaret tax on 94% of the receipts attributed to 304 private parties conducted in the Pavillion Room. The 6% of the receipts excluded from the tax represent expenditures by patrons who are presumed to have left prior [103] to seeing the

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[2]Section 4231(6) imposes "a tax equivalent to 20 per cent of all amounts paid for admission, refreshment, service, or merchandise, at any roof garden, cabaret, or other similar place furnishing a public performance for profit, by or for any patron or guest who is entitled to be present during any portion of such performance. The tax imposed under this paragraph shall be returned and paid by the person receiving such payments * * *"

The term roof garden, cabaret or other similar places is defined by Int. Rev. Code of 1954, Section 4232, to "include any room in any hotel, restaurant, hall, or other public place where music and dancing privileges or any other entertainment, except instrumental or mechanical music alone, are afforded the patrons in connection with the serving or selling of food, refreshment, or merchandise * * *"

Though the operative sections of the Code have been changed during the five-year period for which the tax is assessed, I have referred only to the sections of the 1954 Code since they substantially embody the provisions which are applicable to each period included in the assessment.

show.[3] While there is some variation in the way these 304 parties were conducted, for the most part private organizations would contact Ciro's for the purpose of arranging for the use of the Pavillion Room on a particular night for the exclusive use of its members. A contract would be negotiated and a deposit secured. Generally dinner would be served commencing some time around 7:00 p.m. and terminating before 10:30 p.m. During this period the movable partition separating the Main Room from the Pavillion Room would remain closed and the parties had the complete and uninterrupted privacy of the Pavillion Room to do as they pleased. Depending on the nature of the organization, speeches, awards, community singing, local entertainment or dancing to music either piped in from the Main Room or furnished by their own hired orchestra might follow the dinner. In any event, at approximately 10:30 p.m. [104] the separation was usually removed so as to enable the groups to view the floor show in the Main Room. There seems to be no question but that the patrons attending the dinner in

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[3]Such charges are exempt from the tax under U. S. Treas. Reg. 43, Section 101.13 (b) (1941), which exempts from the tax charges incurred by patrons who do not remain for any part of the performance.

The use of the 94% figure in computing the tax is admittedly an estimate but in view of plaintiff's failure to keep records as provided by law the Government takes the position that it can reasonably carry over and apply the same percentage of those receipts which are non-taxable in the Main Room to the Pavillion Room operation.

the Pavillion Room expected to be able to see the entertainment in the Main Room, it being the understanding, whether committed to writing or not, that the so-called private parties would be afforded this privilege. Upon conclusion of the floor show, the evidence indicates that most of the guests at the private parties left the premises.

It is under these circumstances that I am called upon to construe the meaning of Section 4231(6) which imposes a tax on amounts paid for refreshment or service at a cabaret:

> "* * * furnishing a public performance for profit by or for any person or guest who is entitled to be present during any portion of such performance * * *"

The statute is not free from ambiguity and must be construed so as not to produce illogical or irrational results. A literal translation of the above provision would ascribe to Congressional intent a most arbitrary and unreasonable basis on which the tax is imposed. Such a literal reading of the statute would subject an establishment which operates as a cabaret in the evening to a tax on its late afternoon receipts since it is conceivable that these afternoon patrons might presumably be entitled to view a portion of the evening entertainment if they were to remain on the premises until [105] show time. To condition a tax on such a tenuous showing that the patrons might if they were to wait long enough view the entertainment does not accord with any meaningful or purposeful distinction that we must impute to

Congress. As noted by the Supreme Court, "taxation is an intensely practical matter and laws in respect of it should be construed and applied with a view of avoiding, so far as possible, unjust and oppressive consequences." Farmers Loan Co. v. Minnesota, 280 U. S. 204, 212 (1930). See also Paxson v. Commissioner, 144 F. 2d 772, 776 (C.C.A. 3, 1944). In connection with the present statute the Internal Revenue Bureau itself, through the issuance of interpretive regulations and rulings, has impliedly recognized the necessity, or at least the desirability, of limiting the broad language of the statute.[4]

The Internal Revenue Bureau has taken the position, however, that payments for food, refreshment, service or merchandise made prior to the beginning of the entertainment in a cabaret, roof garden or other similar place by patrons who are entitled to view a public performance are subject to the cabaret tax where the patrons by or for whom such amounts are paid do in fact remain for any [106] portion of the performance. Rev. Rul. 54-487, 1954-2 Cum. Bull. 376. Though limiting somewhat the broad scope and effect which flows from a literal reading of the statute,[5] the revenue ruling nevertheless poses

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[4]See U. S. Treas. Reg. 43, Section 101.13 (b) (1941), supra, note 3.

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[5] This ruling like the Treasury Regulation cited in note 3, supra, precludes taxation of charges incurred by patrons who do not remain for the public performance.

an unrealistic criterion which may in some situations lead to results which under no stretch of the imagination could be considered as within the contemplation of Congress in enacting Section 4231 (6).

The opinion in La Jolla Casa de Manana v. Riddell, 106 F. Supp. 132 (S. D. Cal., 1952) aff'd 206 F. 2d 925 (C.A. 9, 1953), is particularly significant inasmuch as it presumably expresses the Ninth Circuit's thinking on the subject. Judge Byrne, by noting that Congress in imposing a cabaret tax, "envisioned an essential unity between the service of refreshment and the enjoyment of the entertainment," adopted an interpretation inconsistent with that placed on the statute by the Revenue Department (106 F. Supp. at 135). Involved in the Casa de Manana case was the imposition of the cabaret tax from midnight until 2:00 a.m. after the entertainment had ceased. Though some of the patrons to whom refreshments were sold during these hours had been present during part of the entertainment prior to midnight, the Court refused to [107] allow a cabaret tax assessment on any of the receipts from midnight to 2:00 a.m. A contrary decision, as noted by Judge Byrne, would place a construction on the statute which would exempt post midnight purchases by patrons who were present at the entertainment from 9:15 p.m. until 9:30 p.m. and returned at 12:30 a.m., while taxing such purchases by patrons remaining at the cabaret past 12:00 o'clock p.m. The illogic of such a construction is demonstrated by the fact that the applicability of the tax

on post midnight purchases would be made dependent on whether or not a patron would take a walk at midnight. Though the Casa de Manana case concerned itself with the taxability of receipts subsequent to a public performance its underlying rationale is equally applicable to receipts obtained prior to the commencement of such a performance. Using the same reasoning as was employed by Judge Byrne the taxation of all payments made for refreshments and service by patrons who were present both prior to and during the public performance, where the applicability of the tax to the pre-performance receipts would be otherwise had there been an interval in their attendance, is without reason and logic.

I do not mean to suggest that the Treasury Regulations taxing such receipts should be denied any meaning [108] and effect. Certainly, to allow pre-performance receipts in each and every case to escape the imposition of a tax would serve to provide a facile means for tax avoidance, would compound the already existing difficulties present in tax collection and administration, and would be as much productive of inequities and as lacking in logic as would be the adoption of the other extreme —holding all pre-performance payments by persons remaining for the public performance within the pale of this statute. The only sensible and practical approach to the problem is to consider the wording of the statute in the light of each factual situation as it is presented keeping always in mind the ob-

jectives and purposes the statute sought to achieve. As I construe the statute, whatever be its true scope, it was never intended to cover those pre-performance payments by patrons whose desire to be present at the public performance was incidental to some other more cogent reason for attending the cabaret, such as a gathering of a private club or organization for the conduct of its business. Any other construction would lead to some of the strikingly incongruous results suggested by counsel.

In the instant case the chief factor militating against inclusion of the pre-performance receipts in the tax assessment is that the patrons by or for whom the charges [109] were incurred were seemingly members of a private party, a factor which is relevant in showing that their chief motivation for engaging Ciro's was for the purpose of enjoying the intimacy of their own private gathering rather than for purposes of seeing the floor show. In this regard the Government has referred me to U. S. Treas. Reg. 43, Section 101.14 (b) (1941), made applicable to 1954 Code by T. D. 6091, 1954-2 Cum. Bull. 47, which provides that amounts paid for refreshment, service, or merchandise in a room which is entirely separate from the room in which entertainment is furnished, are not subject to tax provided the patrons in such a separate room may not witness the entertainment and any door in the wall or partition separating the two rooms remains closed during the period of entertainment except when persons pass from one room to another. For

similar judicial constructions of the statute see In re Duffin, 141 F. Supp. 869 (S. D. Cal., 1956); McKenzie v. Maloney, 71 F. Supp. 691 (D. Ore., 1946). The Government argues that since the partition was removed at 10:30 p.m. and the Pavillion Room patrons were able to view the entertainment the case does not fall within the exception set out by the regulations and the tax assessment here in issue was entirely proper.

The error of the Government's reasoning [110] lies in its failure to distinguish two separate concepts. The taxing statute requires that there be both (1) a public performance and (2) the patrons be entitled to view any portion of such a performance, as a condition for the imposition of the cabaret tax. The regulation above upon which the Government places such strong reliance goes solely to the question of whether there is a public performance. As a related issue, though nevertheless separate and distinct, is the question of whether or not the patrons of the Pavillion Room were entitled to be present during any of this performance. As noted earlier, "entitled to be present" cannot be construed literally and must be read in the light of the circumstances of each individual case. Even assuming arguendo that in view of the removal of the partition at or about 10:30 p.m. there was a public performance in regard to the Pavillion Room guests it is not determinative of whether such guests were entitled to be present under the meaning which I have ascribed to such words. The fact that the

Pavillion Room parties may have been public when viewed in their entirety is immaterial insofar as it pertains to the pre-performance receipts if it be shown that the main purpose of private groups in engaging the Paviillion Room was other than to be present at the entertainment. To conclude as does the [111] Government that a showing that plaintiff has failed to place himself within the exception of Section 101.14(b) of Regulation 43 is dispositive of the entire issue raised by the tax on the Pavillion Room receipts is susceptible to the same objections raised by Judge Byrne in the Casa de Manana case. Under such a criterion, a day-long convention if held in the Pavillion Room would have its entire payments for services and refreshments subjected to the tax if at 10:30 p.m. the separation was removed for the conventioneers to view for an hour or so the entertainment in common with the public patrons enjoying the facilities of the Main Room; or, perhaps to better illustrate the unsoundness of this position, the Government seeks to sustain the tax imposed, though under the applicable regulations it must concede that if the Pavillion Room parties had been truly private prior to 10:30 p.m. and had the guests thereupon disbanded only to return individually to the Main Room, undistinguished from the other patrons to view the floor show, the charges incurred in the Pavillion Room would not be taxable.

It follows that in the instant case a determination of whether the parties when viewed in their entirety

are public or private cannot be conclusive of the ultimate issue presented. Rather, the applicability of the tax is to be [112] tested by the motivation formulation which I have previously described. In order to determine how significant a factor the privilege of viewing the floor show played in the decision of the 304 organizations to reserve the Pavillion Room, evidence of the operations and physical facilities of both rooms are relevant. Certainly, if the operations and physical layouts of both rooms were such as to give the impression of oneness, the inference is justified that the organizations using the Pavillion Room desired to simulate as much as possible the conditions in the Main Room, considered themselves part and parcel of the general Ciro's operation, and not so much for reasons of privacy but for purposes of capturing Ciro's atmosphere, floor show and all, engaged the facilities of the Pavillion Room.

There seems to be no real dispute that the 304 parties in dispute were private up to 10.30 p.m. The Government concedes that if the parties had ended before the commencement of the floor show or if the partition had remained closed and the Pavillion Room patrons excluded from entering the Main Room or observing the activity therein the expenditures before 10:30 p.m. would not lie within the scope of the tax. This would be true, even if the groups using the Pavillion Room had arranged for their own entertainment since under the statute there would be no public performance. [113]

The crucial determination then, as I see it, is whether the operation of these so-called private parties is so intimately related to the general operation of the Main Room, and the viewing by the Pavillion Room guests of the entertainment at 10:30 p.m. such an integral part of their evening's activities, that it can be reasonably inferred that the compelling motive in reserving the use of the Pavillion Room was for purposes of seeing Ciro's entertainment. On this question much evidence was received at the trial. In addition, in order better to understand and appraise the physical relationship between the two rooms, as I have indicated, the Court itself inspected the premises with all counsel present. On the basis of this personal observation it is my opinion that the floor plan and structural layout of the two rooms compels the finding that two separate and distinct rooms were contemplated by the owner and that it was intended that Ciro's would acquire the private party business by offering the privacy necessary to these organizations in the execution of their customary meetings or gatherings while affording them the opportunity of functioning in a well-known establishment like Ciro's.

The two rooms are separated by a lounge [114] with separate seating and dining facilities. The lounge is slightly elevated and the Pavillion Room is further raised, thereby creating a six step elevation differential between the Pavillion Room and the Main Room. Because of this added height the patrons sitting in the Pavillion Room can view the

entertainment in the Main Room when the separation wall and curtain are withdrawn by looking through the adjacent lounge. However, since the stage is located at the other end of the Main Room, obtaining a good perspective of the floor show from the Pavillion Room is difficult in view of the distance involved, and those in the rear of the Pavillion Room must move their seats into the fore part of that room in order to view the show. Though ingress and egress to both rooms is possible by way of the lounge, the Pavillion Room has in addition its own separate entrance. Rest Rooms are shared in common with the Main Room, though entrance can be made from the Pavillion Room itself. Each room has its separate dance floor and band stand. Tables and chairs used in the respective rooms seem to be of a different character and their arrangement dissimilar. The building plans further disclose that the two rooms were not constructed as one unit but that the Pavillion Room was added long after the Main Room had been in existence. I [115] might further add that upon the closing of the partition separating the two rooms there is an atmosphere of complete privacy and it is reasonable to assume that it was this privacy together with the facilities available at Ciro's which the organizations found so attractive.

A comparison of the respective operations of both rooms further discloses an intent on the part of the management to treat the rooms other than as a single unit. The plaintiff has testified as to some 25 basic differences in the operations of the two rooms. To

mention but a few such distinctions—there were differences in menus, prices, services, working hours and duties of the waiters, manner of payment, parking fees, cover charges, etc. Under such circumstances I find that the private groups availing themselves of the facilities of the Pavillion Room did not consider themselves as part of the public patronage at Ciro's and that any intent on their part of being assimilated into the general overall cabaret atmosphere of Ciro's was of incidental significance in their decision to conduct their parties in the Pavillion Room.[6] Their conscious choice to reserve the Pavillion Room which was located at considerable distance from the main sphere of activity indicates to me that the prime moving consideration in selecting the Pavillion Room was the desire to achieve some sense of privacy for their group activity and business—at least until the entertainment began. In view of this conclusion the receipts prior to the removal of the separation in the Pavillion Room and the commencement of the floor show are outside the scope of the cabaret tax and were improperly included within the assessment.

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[6]I am not unmindful that one of the inducements for arranging such gatherings at Ciro's was the opportunity to view the floor show. But it seems reasonable to me that if such were the principal factor in selecting Ciro's the private groups would have done infinitely better to reserve so many tables in the main entertainment room to accommodate their party. As such they would not only have a much better vantage point from which to see the show but they would be able to use the large dance floor located in the Main Room with less inconvenience.

Plaintiff next contends that if the parties be found to be private prior to 10:30 p.m. such a characterization should not be destroyed upon the removal [117] of the partition, and that all receipts whether obtained prior to or subsequent to the entertainment should be excluded from the tax. Since the evidence is undisputed that upon the removal of the partition the Pavillion Room guests did observe and participate in the public performance in common with the other patrons in the Main Room I fail to see why any distinction between the two rooms is warranted during this period. I might analogize the position of the Pavillion Room guests to the patrons of the lounge during the show or to the late-comers to the Main Room, who because of the crowded conditions existent there, are forced to stand at the bar in the lounge in order to see the floor show. Any payments for drinks or refreshments made by these patrons would, of course, be subject to the tax.

The parties have stipulated that with respect to the $55,581.98 assessed against the Pavillion Room receipts, $5,200.63 would represent the tax on payments made subsequent to 10:30 p.m. I find therefore that $5,200.63 represents the correct tax assessment on the Pavillion Room operation. [118]

Ciroette Room

The Ciroette Room like the Pavillion Room was used primarily to accommodate private gatherings. However, unlike the Pavillion Room, it was located on the second floor of the building and those patrons desiring to see the floor show could do so only by

descending a flight of stairs and passing through two doorways to the Main Room. Contending that plaintiff held out to the prospective organizations desiring to use the Ciroette Room the promise of seeing the entertainment at 10:30 p.m. and that some 5% of the Ciroette patrons did in fact avail themselves of this opportunity the Government assessed a cabaret tax based on 5% of the receipts taken in by the Ciroette Room. Plaintiff concedes that if any tax is due it is to be computed on the basis of 5% of these receipts and the only question presented for my consideration is whether as a matter of law the cabaret tax applies to this 5%.

The nature of these private parties being similar to those conducted in the Pavillion Room my prior discussion on this subject is pertinent here and does not have to be repeated. However, the reasons for denying the tax on pre-performance receipts in the Pavillion Room are even more potent here in view of the obvious remoteness of the Ciroette Room and the substantial effort and distance [119] to be traversed for its patrons to observe the floor show. I find therefore, that the tax assessment on the 5% of the Ciroette Room's receipts is improper.

Closed House Parties

Part of the initial deficiency assessment consists of a 20% tax on all amounts paid for admission, refreshment, service or merchandise on twenty evenings when all the facilities of Ciro's were reserved by and for the members of one particular organization. The Government seeks to sustain the imposi-

tion of the tax on the basis of a recent ruling which reads as follows:

"Where a private organization arranges to hold an affair in a room at a hotel which normally is operated as a cabaret and the affair is held under such circumstances that the hotel furnishes practically the same services, including entertainment, during the same hours that the room is operated as a cabaret, the arrangements made by the private organization are regarded as a mere reservation of tables. In such case, the Bureau holds that the room is operated as a cabaret on such occasions, even though the patronage is limited to the members, together with the guests of the private organization, and the private organization furnishes entertainment in addition to that furnished by the hotel * * *

Where a private organization holds a dinner in a room at a hotel, under such circumstances that the hotel does not furnish any entertainment but the private organization does provide dancing facilities for the persons [120] attending by hiring an orchestra, or furnishes other entertainment, cabaret tax does not apply to any amount paid in connection with the affair." Special Ruling, August 31, 1949, 5 CCH 1950 Stand. Fed. Tax Rep. Para. 6053.

Under this ruling the issue to be resolved is whether the same services and entertainment were provided or whether the private organizations themselves contracted for the entertainment. The ruling by the Commissioner has never been passed on by a Court and plaintiff contends that it is contrary to

those cases which determine the applicability of the tax on the basis of whether the parties are public or private. See United States vs. Lambeth, 176 F. 2d 810 (C.A. 9, 1949); Naylor vs. United States, 102 F. Supp 309 (S.D. Cal. 1952). Under plaintiff's interpretation of the law the taxability of the receipts in question hinges on a determination of whether the public was in fact excluded from these parties.

The respective litigants are therefore in hopeless conflict on the applicable criteria to be applied. However, I need not resolve this conflict in order to dispose of the immediate issue before me. Even assuming the correctness of the Government's position, it cannot prevail since the evidence conclusively establishes that the private [121] organizations themselves contracted for the entertainment and music. I attach little significance to the fact that the show usually provided was the same as that regularly staged by Ciro's and that Ciro's advised the private organizations as to the amount and distribution of the payments to be made to the performers if the private organizations should hire them. It appears, that at best, Ciro's was acting as an intermediary for the convenience of the private groups. The evidence is unmistakably clear that in all cases payments were made directly by the private groups to the performers and private groups could if they so desired rent the Main Room without the Ciro entertainment and could furnish instead their own entertainment and orchestra. Indeed when the Ciro entertainers were retained by the private groups they

were able to exercise control over the time when the performers would commence, the type of performance, etc., indicating it was a closed private group performance. As such, any service rendered by Ciro's was purely advisory and for the convenience of the private group and does not justify a finding that Ciro's furnished the entertainment on these twenty evenings in issue. The private organizations remained free to reject the regular entertainment appearing at Ciro's and if they chose to engage such performers could modify their [122] acts to suit their own purposes.

The Government's contention that on six of the twenty nights in question the public was admitted and as to at least these six occasions all the receipts should be taxable equally, is without merit. It appears that the public was admitted only after the private groups had concluded their parties and surrendered the premises. The subsequent reversion of the Club to a cabaret status can certainly have no bearing on the nature or the character of the parties in which the public was rigidly excluded.

I find that the assessment on the twenty closed house parties is improper. Submit judgment consistent with this opinion.

Dated: January 3, 1958.

/s/ IRVING R. KAUFMAN,
United States District Judge.

[Endorsed]: Filed January 3, 1958. [123]

[Title of District Court and Cause.]

MOTION FOR NEW TRIAL

Defendant, United States of America, through its counsel of record, moves the Court for an order vacating and setting aside the judgment dated, filed and entered January 3, 1958, and for a new and further trial, or for a judgment in favor of the defendant as prayed for in the defendant's answer and counterclaim, upon the following grounds:

(1) The conclusions of law and judgment entered therein are contrary to and inconsistent with the findings of fact found by the Court to be true.

(2) Error in law occurring at the trial in entering judgment in favor of the plaintiff on all issues except the sale of drinks in the Pavillion Room after 10:30 p.m., instead of in entering judgment for defendant upon the findings of fact which were found to be true by the Court. [124]

(3) Insufficiency of the evidence to justify the following findings:

(a) Upon conclusion of the floor show, most of the guests at the private parties of the Pavillion Room left the building.

(b) The patrons by or for whom the charges in the Pavillion and Ciroette Rooms were incurred were seemingly members of private parties.

(c) The 304 parties in dispute with respect to the Pavillion Room were private up to 10:30 p.m.

(d) The operation of these so-called private parties is not so intimately related to the general operation of the Main Room, and the viewing by the Pavillion Room guests of the entertainment at 10:30 p.m. such an integral part of their evening's activities, that it can be reasonably inferred that the compelling motive in reserving the use of the Pavillion Room was for the purposes of seeing Ciro's entertainment.

(e) That the private groups availing themselves of the facilities of the Pavillion Room did not consider themselves as part of the public patronage of Ciro's and any intent on their part of being assimilated into the general overall cabaret atmosphere of Ciro's was of incidental significance in their decision to conduct their parties in the Pavillion Room.

(f) The receipts prior to the removal of the separation in the Pavillion Room and the commencement of the floor show are out side the scope of the cabaret tax and were improperly included within the assessment.

(g) That $5,200.63 represents the correct tax assessment on the Pavillion Room operation.

(h) That the amount of drinks served after 10:30 p.m. rather than the payments received for food, refreshment and merchandise, whenever sold, represents the correct measure of [125] cabaret tax liability.

(i) That the tax assessment on 5% of the Ciroette Room receipts is improper.

(j) With respect to the Closed House parties the entertainment was furnished by the private groups rather than by Ciro's.

(k) That Ciro's did not furnish the entertainment on the 20 evenings in issue.

(l) That on 6 of the 20 nights in question the private groups had concluded their parties and surrendered the premises before the general public was admitted.

(4) With respect to the various issues, the Court failed to find based on the weight of the evidence that the payments made by the patrons of the Pavillion Room and 5% of the patrons of the Ciroette Room entitled them to be present at public performances for profit and thus subjected to the tax their payments for food, refreshment and merchandise during the evidence they were at Ciro's.

(5) Error in law occurring at the trial and insufficiency of the evidence to justify the finding that the showing that plaintiff has failed to place himself within the exception of Section 101.14(b) of Regulation 43 is not dispositive of the entire issue raised by the tax upon the Pavillion Room receipts.

The motion will be made and based upon the following papers:

(a) The Complaint.

(b) Amended answer and counterclaim.

(c) Defendant's memorandum of law.

(d) Defendant's pre-trial opening statement.

(e) Reply to counterclaim. [126]

(f) Stipulation of Facts.

(g) Stipulation re the cumulative effect of the testimony of Pavillion Room witnesses.

(h) Brief of the United States.

(i) Court's decision filed January 3, 1958.

(j) All exhibits.

(k) Reporter's transcript of the testimony.

With respect to ground 3 of the motion and its subdivisions, the great preponderance of the evidence of the many and various witnesses who are unbiased and credible in every regard was contrary to the facts found. The plaintiff's testimony is entitled to little weight and credence because of his bias and obvious interest in the outcome of the suit and of his failure to recall the details of any particular banquet party, and for the further reason of his failure to call any other or supporting witnesses with respect to the matters to which he testified.

Respectfully submitted,

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant United States Attorney, Chief, Tax Division,

/s/ EDWARD R. McHALE,
Attorneys for Defendant. [127]

Memorandum in Support of Motion for New Trial

A new trial may be granted on all or part of the issues in an action tried without a jury, for any of the reasons for which rehearings have heretofore been granted in suits in equity in the courts of the United States. On a motion for a new trial in an action tried without a jury, the Court may open the judgment if one has been entered, take additional testimony, amend findings of fact and conclusions of law, or make any findings and conclusions, and direct the entry of a new judgment.

Fed. R. Civ. P. 59(a).

Fed. R. Civ. P. 59(b).

Local Rules for the Southern District of California, Rule 17.

Affidavit of Service by Mail attached.

[Endorsed]: Filed January 13, 1958. [128]

[Title of District Court and Cause.]

PROPOSED FINDINGS OF FACT, CONCLUSIONS OF LAW AND JUDGMENT

The above cause came on regularly for trial on December 19, 1957, before the Honorable Irving R. Kaufman, United States District Judge, presiding, without the intervention of a jury, the plaintiff represented by his attorney, Ernest R. Mortenson,

Esq., the defendant represented by its attorneys, Laughlin E. Waters, United States Attorney, and Edward R. McHale, Assistant United States Attorney, Chief, Tax Division; and after having been continued for further trial from time to time, and evidence received, briefs filed, and oral arguments having been heard, and having on December 26, 1957, been duly submitted, and the Court having duly considered the evidence, briefs and arguments of the parties, and having on January 3, 1958, filed its opinion, now finds as follows:

Findings of Fact

I.

On November 14, 1955, the authorized delegate of the Secretary of the Treasury assessed against Herbert D. Hover, d/b/a [130] Ciro's, cabaret taxes for the period June 1, 1951, through March 31, 1955, in the sum of Sixty-seven Thousand Six Hundred Sixty Dollars and Sixty-two Cents ($67,660.62) taxes and Seven Thousand Eight Hundred Fifty-eight Dollars and Fifty-one Cents ($7,858.51) interest for a total assessment of Seventy-five Thousand Five Hundred Nineteen Dollars and Thirteen Cents ($75,519.13). Notice and demand for payment of the said taxes and interest was made upon the plaintiff on November 16, 1955, and he paid the sum of Three Hundred Dollars ($300.00), and no more, on August 7, 1956, leaving an outstanding balance of said assessment of Seventy-five Thousand Two Hundred Nineteen Dollars and Thirteen Cents

($75,219.13), together with interest as provided by law.

II.

The aforesaid deficiency assessment of cabaret taxes represented additional taxes assessed with respect to three phases of plaintiff's operation for the period involved: The Ciroette Room; the Pavillion Room and the "Closed House" parties. Of the total assessment of Sixty-seven Thousand Six Hundred Sixty Dollars and Sixty-two Cents ($67,-660.62), Nine Hundred Ninety-two Dollars ($992.00) is attributable to "Main Room operations" and is conceded to be due and owing by the plaintiff because of a clerical error and is not in issue in this lawsuit.

III.

The amounts of the respective deficiencies in tax determined by the Revenue Agents who made the audit, was based on their examination of plaintiff's books and records and applied the cabaret tax to a certain percentage of the receipts of each room on a basis that is more fully detailed hereinafter. The taxpayer did not consider the receipts here in issue of the said rooms taxable and, consequently did not, in his books and records, segregate any portion of the receipts as Federal cabaret taxes. [131]

IV.

Plaintiff maintained records showing receipts and the computation of the cabaret tax as reported on the tax returns, but plaintiff kept no records showing what, if any, proportion of the persons who at-

tended the parties in the Pavillion Room stayed for the floor show or for dancing.

V.

Ciro's, located on Sunset Boulevard in Los Angeles, is subdivided into three rooms in which the services and facilities of the Club are offered to the public. In addition to the main entertainment and dining room, herein referred to as the "Main Room," there are the "Pavillion" and "Ciroette" rooms. A lounge or cocktail bar located adjacent to the Main Room also serviced Ciro's patrons but its operations are not involved in this suit. In issue in this proceeding are the taxability of receipts from (1) the Pavillion Room, (2) the Ciroette Room and (3) the "Closed House parties"—when the entire club was closed to the public and reserved for the exclusive use of private organizations.

VI.

The Pavillion Room is located adjacent to the lounge (which is basically a raised extension of the Main Room) and is separated therefrom by a movable wall and thick, soundproof curtain. This room was used primarily to accommodate private organizations which desired to reserve for the evening such a room for the exclusive use of its members.

VII.

The Government assessed a cabaret tax on 94% of the receipts attributed to 304 private parties conducted in the Pavillion Room. The 6% of the re-

ceipts excluded from the tax represents amounts paid for food, refreshment or merchandise by or for patrons or guests who are presumed to have left prior to seeing the floor show. [132]

VIII.

While there is some variation in the way these 304 parties were conducted, for the most part private organizations would contact Ciro's for the purpose of arranging for the use of the Pavillion Room on a particular night for the exclusive use of its members. A contract would be negotiated and a deposit secured. Generally dinner would be served commencing some time around 7:00 p.m. and terminating before 10:30 p.m. During this period the movable partition separating the Main Room from the Pavillion Room would remain closed and the parties had the complete and uninterrupted privacy of the Pavillion Room to do as they pleased. Depending on the nature of the organization, speeches, awards, community singing, local entertainment or dancing to music either piped in from the Main Room or furnished by their own hired orchestra might follow the dinner. In any event at approximately 10:30 p.m. the separation was usually removed so as to enable the groups to view the floor show in the Main Room.

IX.

The patrons attending the dinner in the Pavillion Room expected to be able to see the entertainment in the Main Room, it being the understanding,

whether committed to writing or not, that the so-called private parties would be afforded this privilege. Upon conclusion of the floor show, most of the guests at the private parties left the premises.

X.

In view of the removal of the partition at or about 10:30 p.m., there was a public performance in regard to the Pavillion Room guests from that time on.

XI.

The 304 parties in dispute were private up to 10:30 p.m.

XII.

Ciro's was a famous night club, offering top-notch entertainers [133] for its floor shows, such attractions as Sammy Davis, Jr., Sophie Tucker, Xavier Cugat and his orchestra, and it attracted noted Hollywood personalities as its customers. It offered dancing nightly to two alternating orchestras in the Main Room. Ciro's widely advertised its entertainment.

XIII.

In its advertising Ciro's offered the facilities of the Ciroette Room and the Pavillion Room to banquet groups with the inducement that the groups could witness the famed Ciro's entertainment.

XIV.

The operation of the so-called private parties was related to the general operation of the Main Room.

XV.

The viewing by the Pavillion Room guests of Ciro's entertainment after 10:30 p.m. was an integral part of their evening's activities and was a motive in reserving the use of the Pavillion Room.

XVI.

The construction of the Pavillion Room was planned and executed by the plaintiff after he had been operating Ciro's for some years, with one of the major features being the expansion of the banquet business by the ability to offer the famed Ciro's entertainment to regular banquet groups without their being obliged to leave the room they dined in and by Ciro's not being obliged to put on an extra performance in a separate room for the banquet groups.

XVII.

The floor plan and structural layout of the Main Room and the Pavillion Room compels the finding that two separate and distinct rooms were contemplated by Mr. Hover and that it was intended that Ciro's would acquire the private party business by offering the privacy necessary to these organizations in the execution of their [134] customary meetings or gatherings while affording them the opportunity of functioning in a well-known establishment like Ciro's and witnessing the famed entertainment provided for its Main Room customers at the same time and with the same glamorous atmosphere.

XVIII.

The two rooms are separated by a lounge with separate seating and dining facilities. The lounge is a slightly elevated portion of the Main Room and the Pavillion Room is further raised, thereby creating a six step elevation differential between the Pavillion Room and the Main Room. Because of this added height the patrons sitting in the Pavillion Room can view the entertainment in the Main Room when the separation wall and curtain are withdrawn by looking through the adjacent lounge. Since the stage is located at the other end of the Main Room, obtaining a good perspective of the floor show from all portions of the Pavillion Room is difficult in view of the distance involved, and those in the rear of the Pavillion Room must move their seats into the fore part of that room in order to view the show. Though ingress and egress to both rooms is possible by way of the lounge, the Pavillion Room has in addition its own separate entrance. Rest Rooms are shared in common with the Main Room, though entrance can be made from the Pavillion Room itself. Each room has its separate dance floor and band stand. Tables and chairs used in the respective rooms seem to be of a different character and their arrangement dissimilar. The building plans further disclose that the two rooms were not constructed as one unit but that the Pavillion Room was added long after the Main Room had been in existence. Upon the closing of the partition separating the two rooms there is an atmosphere of complete privacy.

XIX.

This privacy together with the facilities and entertainment available at Ciro's was found attractive by the organizations. [135]

XX.

Of the 304 known evenings during the period involved when the Pavillion Room was engaged by banquet groups, on 257 of those occasions the price of drinks sold to the Pavillion Room patrons was raised from 75 cents to 90 cents at show time, an increase of 20 per cent. No part of the price of the drinks sold therein was either reported as cabaret tax, set aside as cabaret tax by the plaintiff, or paid over to the United States as cabaret tax.

XXI.

It was the general understanding of the groups using the Pavillion Room that the increase in the price of the drinks from 75 cents to 90 cents at show time was caused by the collection of the cabaret tax; indeed, Ciro's encouraged that belief both orally and in writing.

XXII.

Plaintiff did not maintain any records to show and has not shown the amounts paid for refreshments, service, and merchandise by or for the patrons or guests of the Pavillion Room who either:

(a) Saw and heard the floor show and dancing in the Main Room from the Pavillion Room;

(b) During a portion of the evening went into the main diding room to dance;

(c) During a portion of the evening went into the Main Room to witness or hear a portion of the entertainment; or

(d) Who left Ciro's before show time and before the accordion curtain was opened.

XXIII.

A comparison of the respective operations of both rooms further discloses an intent on the part of the management to treat the rooms other than as a single unit. The plaintiff has testified as to some 25 basic differences in the operations of the two rooms. To mention but a few such distinctions—there were differences in [136] menus, prices, services, working hours and duties of the waiters, manner of payment, parking fees, cover charges, etc.

XXIV.

The private groups availing themselves of the facilities of the Pavillion Room had an intent on their part of being assimilated into the general overall cabaret atmosphere of Ciro's.

XXV.

Said intent was of incidental significance in their decision to conduct their parties in the Pavillion Room.

XXVI.

Said groups did not consider themselves as part of the public patronage at Ciro's.

XXVII.

Their conscious choice to reserve the Pavillion Room which was located at considerable distance from the main sphere of activity indicates that the prime moving consideration in selecting the Pavillion Room was the desire to achieve some sense of privacy for their group activity and business—at least until the entertainment began.

XXVIII.

Upon the removal of the partition at show time, the Pavillion Room guests did observe and participate in the public performance in common with the other patrons in the Main Room and no distinction between the two rooms is warranted during this period. The position of the Pavillion Room guests is analogous to the patrons of the lounge during the show or to the late comers to the Main room, who, because of the crowded conditions existent there, are forced to stand at the bar in the lounge in order to see the floor show. Any payments for drinks or refreshments made by these patrons were, of course, subject to the tax.

XXIX

Plaintiff has not established the time when payment was [137] actually made by or for the patrons or guests of the Pavillion Room on any of the 304 occasions, for any of the following:

(a) The food served;

(b) The drinks served before dinner; or

(c) The drinks served during dinner.

The plaintiff has established that the drinks served after dinner and after the commencement of show time were paid for at that time, and the cabaret tax applicable thereto was $5,200.63.

XXX.

With respect to the $55,581.98 assessed against the Pavillion Room receipts, $5,200.63 would represent the tax on food, refreshment or merchandise served to patrons or guests subsequent to 10:30 p.m.

XXXI.

No admission charge was made to enter the Main Room from either the Ciroette Room or the Pavillion Room.

XXXII.

The Ciroette Room like the Pavillion Room was used primarily to accommodate private gatherings. However, unlike the Pavillion Room, it was located on the second floor of the building and those patrons desiring to see the floor show could do so only by descending a flight of stairs and passing through two doorways to the Main Room.

XXXIII.

The plaintiff held out to the prospective organizations desiring to use the Ciroette Room the promise of seeing the entertainment at 10:30 p.m. Some 5% of the Ciroette patrons did in fact avail themselves of this opportunity. The Government assessed a cabaret tax based on 5% of the receipts taken in by the Ciroette Room.

XXXIV.

Plaintiff concedes that if any tax is due it is to be [138] computed on the basis of 5% of these receipts and the only question presented for consideration is whether as a matter of law the cabaret tax applies to this 5%.

XXXV.

The nature of these private parties being similar to those conducted in the Pavillion Room, the prior findings on this subject are pertinent here and incorporated by reference. However, the reasons for denying the tax on pre-performance receipts in the Pavillion Room are even more potent here in view of the obvious remoteness of the Ciroette Room and the substantial effort and distance to be traversed for its patrons to observe the floor show.

XXXVI.

Part of the initial deficiency assessment consists of a 20% tax on all amounts paid for admission, refreshment, service or merchandise on twenty evenings when all the facilities of Ciro's were reserved by and for the members of one particular organization, referred to for convenience as "Closed House" parties.

XXXVII.

On the "Closed House" occasions, the show and orchestras usually provided were the same as was regularly staged by Ciro's and Ciro's advised the private organizations as to the amount and distribution of the payments to be made to the performers

if the private organizations should hire them. On none of the 20 occasions in issue did the representatives of the private organizations directly deal with the entertainers or their theatrical agents; instead, they dealt through Ciro's personnel, agreeing to pay for the music and entertainment the price Ciro's personnel fixed. In addition to the 20 occasions in issue, during the period involved in this lawsuit there were some 14 other occasions in which private organizations held "Closed House" parties at Ciro's in which representatives of the organization either negotiated directly with Ciro's entertainers or other entertainers, which occasions the defendant did not treat as [139] taxable.

XXXVIII.

In all cases checks in payment were made payable by the private groups to the performers. Private groups could if they so desired rent the Main Room without the Ciro entertainment and could furnish instead their own entertainment and orchestra. On none of the twenty occasions in issue did they do so. Indeed, when the Ciro entertainers were retained by the private groups they were able to exercise control over the time when the performers would commence and the type of performance. Any service rendered by Ciro's was purely advisory and for the convenience of the private group.

XXXIX.

Ciro's did not furnish the entertainment on these

twenty evenings in issue. The private organizations remained free to reject the regular entertainment appearing at Ciro's and if they chose to engage such performers, could modify their acts to suit their own purposes. In none of the twenty instances in issue did they reject the regular entertainment.

XL.

Although on 6 of the 20 nights in question, the public was admitted, the public was admitted only after the private groups had concluded their private parties and surrendered the premises. The public then witnessed the same entertainment that had been paid for by checks of the private organizations to the management of Ciro's and enjoyed the same entertainment, which in each of the six instances in issue was the same entertainment regularly provided by Ciro's during the period involved.

Conclusions of Law

And from these facts the Court concludes as follows:

I.

The statute imposing the cabaret tax is not intended to cover those pre-performance parties by those patrons whose desire to [140] be present at the public performance was incidental to some more cogent reason for attending the cabaret performance, such as a gathering of a private group or organization for the conduct of its business.

II.

The words "entitled to be present" in the statute do not apply to the Pavillion Room parties where the main purpose of the parties engaging the Pavillion Room was other than to be present at the entertainment.

III.

The criteria of taxability is not whether the amounts paid by or for patrons of the Pavillion Room for food, refreshment and merchandise entitled them to be present during a portion of a public performance for profit or whether the parties when viewed in their entirety are public or private but whether the motive of the private groups engaging the private room was other than to be present at the entertainment.

IV.

If the parties had ended before the commencement of the floor show or if the partition had remained closed and the Pavillion Room patrons excluded from entering the Main Room or observing the entertainment therein, the expenditures before 10:30 p.m. would not lie within the scope of the tax, even if the group using the Pavillion Room had arranged for their own entertainment, since under the statute there would be no public performance.

V.

Although the plaintiff kept no records showing the amount paid after 10:30 p.m. for food, refreshments

or merchandise by or for patrons or guests of the Pavillion Room, it is clear from the evidence presented that the serving of food was completed before the beginning of the floor show. Further, it has been stipulated as to the proportion of the beverages served before and after show [141] time. It is also clear that the bar receipts were paid in cash at the time of service. The $5,200.63 representing the tax on drinks served after 10:30 p.m., is equivalent to the tax on the amounts paid for food, refreshment, and merchandise by or for patrons or guests of the Pavillion Room entitled to be present during such performance for profit and is the correct amount of tax on the Pavillion Room operation. From these facts the Court concludes that of the amount assessed against the plaintiff with respect to the Pavillion Room, the amount representing the service of drinks after 10:30 p.m., in the sum of $5,200.63, is the proper tax on amounts paid by or for patrons or guests of the Pavillion Room for food, refreshment or merchandise after 10:30 p.m.

VI.

The tax assessment on 5% of the Ciroette Room's receipts is improper.

VII.

The private organizations themselves contracted for the entertainment and music supplied to the "Closed House" parties. At best, Ciro's was acting as an intermediary for the convenience of the pri-

vate groups in making the arrangements for the entertainment and music furnished.

VIII.

After the private groups had concluded their parties and surrendered the premises, the club subsequently reverted to a cabaret status and this has no bearing on the nature of the parties from which the public was rigidly excluded.

IX.

With respect to the "Closed House" parties, the payments received by Ciro's did not entitle the patrons or guests to be present during public performances for profit.

X.

Defendant is entitled to judgment on its counterclaim for [142] the tax on the amounts paid for refreshment in the Pavillion Room after 10:30 p.m. and for its costs.

Judgment

In accordence with the foregoing findings of fact and conclusions of law, It is Ordered, Adjudged and Decreed:

(1) That plaintiff take nothing by his complaint for refund of $300.00, and that it be dismissed with prejudice;

(2) That defendant have judgment against plaintiff on its counterclaim for the sum of

$....., together with interest on this judgment until paid according to law and for its costs to be taxed by the Clerk of the Court in the sum of $.....

Dated: This .... day of February, 1958.

.....,
United States District Judge.

Receipt of copy acknowledged.

Lodged: February 14, 1958. [143]

[Title of District Court and Cause.]

MEMORANDUM FOR COMPUTATION OF JUDGMENT

[Local Rule 7(h)]

Pursuant to Local Rule 7(h), defendant files this memorandum of amount to be inserted in the judgment. If the judgment is signed on February 25, 1958, the amount that should be entered in the space provided in line 9, page 14 of the Judgment, is $7,463.86. Interest accrues at the rate of $1.09 per day from February 25, 1958, and appropriate additions should be made to said amount to be inserted in said space in the event the Court signs the judgment after February 25, 1958.

The amount due was computed as follows: [144]

Computation of Tax

Tax due defendant pursuant to Findings ¶¶ XXIX and XXX, and Conclusion ¶ V		$5,200.63
Tax due concededly defendant—clerical error, Finding ¶ II		992.00
Total tax due defendant		$6,192.63
Less: Payment of Aug. 7, 1956, Finding ¶ I		300.00
Net tax due defendant		$5,892.63

Computation of Interest

(1) Proper assessed interest per decision: On $6,192.63, from respective due dates of deficiencies to assessment date of 11/15/55		$ 662.70
(2) Interest from 11/15/55 to 8/7/56		
On all tax	$6,192.63	
On interest assessed against taxes arising under 1939 Code*	647.12	
	$6,839.75	299.24
(3) Interest from 8/7/56 to 2/25/58		
On net tax and assessed interest as above (2)	$6,839.75	
Less—payment of 8/7/56	300.00	
	$6,539.75	609.29
Total interest to 2/25/58		$1,571.23
Net tax due (per above)		5,892.63
Amount to be inserted in Judgment, page 14 line 9, if signed 2/25/58		$7,463.86

*No interest is computed on assessed interest on taxes arising under 1954 Code, § 6601(f)(2), i.e., on $15.58 interest assessed against $479.52 tax for first quarter 1955.

Interest at the rate of $1.09 per day from February 25, 1958, is accruing on $6,539.75 and is to be added to the foregoing sum depending on the date the judgment is actually signed.

Respectfully submitted,

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant United States Attorney, Chief, Tax Division,

/s/ EDWARD R. McHALE,
Attorneys for Defendant,
United States of America.

Approved as to form, pursuant to Local Rule 7(a).

Dated: February 14, 1958.

/s/ ERNEST R. MORTENSON,
Attorney for Plaintiff.

Receipt of copy acknowledged.

[Endorsed]: Filed February 14, 1958. [146]

[Title of District Court and Cause.]

OBJECTIONS TO PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

Pursuant to local Rule 7(a), Plaintiff moves the Court to substitute the following paragraphs for

those contained in Defendant's proposed Findings of Fact, Conclusions of Law and Judgment.

1. Omit Findings of Fact No. XV.

   Reason: This finding is contained in other paragraphs.

2. Omit Finding of Fact No. XVI.

   Reason: The evidence does not justify a finding expressed in these words.

3. Amend Finding of Fact No. XVII to read as follows:

"The floor plan and structural layout of the Main Room and the Pavillion Room compels the finding that two separate and distinct rooms were contemplated by Mr. Hover and that it was intended that Ciro's would acquire the private party business by offering the privacy necessary to these organizations in the execution of [147] their customary meetings or gatherings while affording them the opportunity of functioning in a well-known establishment like Ciro's."

   Reason: The above wording is consistent with the facts stated in the Opinion.

4. Amend Finding of Fact No. XIX to read as follows:

"This privacy together with the facilities available at Ciro's was found attractive by the organizations."

   Reason: The above wording is consistent with the facts stated in the Opinion.

5. Omit Finding of Fact No. XX.

Reason: The parties stipulated as to the amount of tax on sales of refreshment, service and merchandise after 10:30 p.m. Since the drinks were increased to 90 cents after 10:30 p.m., the stipulation covers that matter. With respect to the sales of drinks at 75 cents prior to 10:30 p.m., the Court holds that such sales were not taxable.

6. Omit Finding of Fact No. XXI.

Reason: The evidence regarding the "general understanding" in this regard was conflicting. The proposed finding would not be justified in the light of all of the evidence.

7. Omit Finding of Fact No. XXII.

Reason: The Court has held that the amounts paid after 10:30 p.m. were taxable and the amounts paid before 10:30 p.m. are not taxable. Accordingly, the proposed finding would be entirely irrelevant.

8. Amend Finding of Fact No. XXIV to read as follows:

"The private groups availing themselves of the facilities of the Pavillion Room had no intent on their part of being assimilated in the general overall cabaret atmosphere of Ciro's."

Reason: The proposed Finding of Fact is consistent with the Court's Opinion (bottom page 16, typewritten copy). [148]

9. Omit Finding of Fact No. XXV.

Reason: See reason for change of previous paragraph.

10. Omit Finding of Fact No. XXIX.

Reason: During the course of the trial it was pointed out that the actual time of payment has no relationship to taxability. Payment is often made days or weeks after the event where the patron has a Diners' Club or regular credit card.

11. Amend Finding of Fact No. XXXIII to read as follows:

"Some 5% of the Ciroette patrons saw the entertainment at 10:30 p.m. The Government assessed a cabaret tax based on 5% of the receipts taken in by the Ciroette Room."

Reason: In the Opinion (page 19) part of the proposed Finding was given as a contention of the Defendant. The above amendment properly expresses a Finding which is consistent with the Stipulation regarding the 5% figure.

12. Omit Finding of Fact No. XXXVII.

Reason: The first part of this Finding is contrary to the facts contained in the Opinion. With regard to the fourteen other occasions in which private organizations held "closed house" parties, the tax there involved is not in issue in this proceeding.

13. Amend Finding of Fact No. XXXVIII to read as follows:

"In all cases checks in payment were made payable by the private groups to the performers. Private groups could, if they so desired, rent the Main Room without the Ciro entertainment and could furnish instead, their own entertainment and orchestra. Indeed, when the Ciro entertainers were retained by the private groups they were able to exercise control over the time when the performers would commence and the type of performance. Any service rendered by Ciro's was purely advisory and for the convenience of the private group."

Reason: The above amendment is consistent with the facts appearing in the Opinion (page 22). Mr. Hover testified [149] that the private groups generally had special entertainment to suit the occasion.

14. Amend Finding of Fact No. XXXIX to read as follows:

"Ciro's did not furnish the entertainment on these twenty evenings in issue. The private organizations remained free to reject the regular entertainment appearing at Ciro's and if they chose to engage such performers, could modify their acts to suit their own purposes."

Reason: See reason for amendment of previous paragraph.

15. Amend Finding of Fact No. XL to read as follows:

"Although on 6 of the 20 nights in question, the public was admitted, the public was admitted only

after the private groups had concluded their private parties and surrendered the premises."

Reason: There is no competent evidence to establish what entertainment was given in the 6 instances referred to.

16. Amend Conclusions of Law No. 1 to read as follows:

"The statute imposing the cabaret tax is not intended to cover those pre-performance parties by those patrons whose desire to be present at the public performance was incidental to some more cogent reason for attending the cabaret such as a gathering of a private group or organization for the conduct of its business."

Reason: The insertion of the word "performance" in the proposed finding distorts the meaning of the words in the Opinion at page 9.

17. Omit Conclusion of Law No. III.

Reason: This paraphrasing does not appear to completely state the conclusion set forth in the Opinion.

Respectfully submitted,

/s/ ERNEST R. MORTENSON,
Attorney for Plaintiff.

Dated: 19th day of February, 1958.

Affidavit of Service by Mail attached.

[Endorsed]: Filed February 20, 1958. [150]

[Title of District Court and Cause.]

DEFENDANT'S REPLY TO THE OBJECTIONS TO PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

Pursuant to Local Rules 3(d) and 7, defendant files this reply to plaintiff's objections to the proposed findings of fact and conclusions of law. For convenience, the paragraph numbers of this reply correspond to the paragraph numbers of the objections.

1.

Proposed Finding XV. The viewing by the Pavillion Room guests of Ciro's entertainment after 10:30 p.m. was an integral part of their evening's activities and was a motive in reserving the use of the Pavillion Room.

Plaintiff does not deny the truth of finding but merely states that it is contained in other paragraphs. He has not stated in what other paragraph said finding is contained. It is submitted that said finding is not stated elsewhere in the findings and is an appropriate finding based upon the evidence in accordance with the Court's Opinion. The particular finding is [152] implicit in the first paragraph of page 14 of the Opinion.

2.

Proposed Finding XVI. The construction of the Pavillion Room was planned and executed by the plaintiff after he had been operating Ciro's for

some years, with one of the major features being the expansion of the banquet business by the ability to offer the famed Ciro's entertainment to regular banquet groups without their being obliged to leave the room they dined in and by Ciro's not being obliged to put on an extra performance in a separate room for the banquet groups.

Plaintiff's only objection to paragraph XVI is that the evidence does not justify "a finding expressed in these words." Plaintiff has not suggested an alternative wording. It is submitted that all of the facts herein contained are true and are fully supported by the evidence. Any disagreement with the form proposed should be accompanied with an alternative wording. In the absence of any such alternative wording, the Court should approve the finding as proposed.

3.

Proposed Finding XVII. The floor plan and structural layout of the Main Room and the Pavillion Room compels the finding that two separate and distinct rooms were contemplated by Mr. Hover and that it was intended that Ciro's would acquire the private party business by offering the privacy necessary to these organizations in the execution of their customary meetings or gatherings while affording them the opportunity of functioning in a well-known establishment like Ciro's and witnessing the famed entertainment provided for its Main Room customers at the same time and with the same glamorous atmosphere.

Plaintiff makes no objection to the last clause of paragraph XVII, merely stating that the first portion of the paragraph is consistent with the facts stated in the Opinion. [153] Since the plaintiff has not articulated any reasons for the objection to the last phrase, and the evidence fully supports the facts found there, it is suggested that said finding should be approved by the Court.

4.

Proposed Finding XIX. This privacy together with the facilities and entertainment available at Ciro's was found attractive by the organizations.

Likewise in paragraph XIX, the plaintiff fails to articulate any objection to the words "and entertainment" contained in lines 30 and 31 of page 6. It is submitted that the evidence is quite clear that the entertainment offered at show time was found to be attractive by the organizations. Said finding should be made as offered.

5.

Proposed Finding XX. Of the 304 known evenings during the period involved when the Pavillion Room was engaged by banquet groups, on 257 of those occasions the price of drinks sold to the Pavillion Room patrons was raised from 75 cents to 90 cents at show time, an increase of 20 per cent. No part of the price of the drinks sold therein was either reported as cabaret tax, set aside as cabaret tax by the plaintiff, or paid over to the United States as cabaret tax.

Plaintiff objects to finding XX presumably on the grounds that the facts were stipulated. However, the Court should be reminded that said finding supports the Court's determination with respect to the taxability of the receipts after 10:30 p.m. and the defendant is entitled to have such a finding formally made, particularly, when it is fully supported by the evidence.

6.

Proposed Finding XXI. It was the general understanding [154] of the groups using the Pavillion Room that the increase in the price of the drinks from 75 cents to 90 cents at show time was caused by the collection of the cabaret tax; indeed, Ciro's encouraged that belief both orally and in writing.

The same reasoning applies with respect to paragraph XXI and its inclusion as applies to paragraph XX heretofore discussed in paragraph 5. Furthermore, it is urged that the preponderance of the evidence fully supports the finding.

7.

Proposed Finding XXII. Plaintiff did not maintain any records to show and has not shown the amounts paid for refreshment, service, and merchandise by or for the patrons or guests of the Pavillion Room who either:

(a) Saw and heard the floor show and dancing in the Main Room from the Pavillion Room;

(b) During a portion of the evening went into the main dining room to dance;

(c) During a portion of the evening went into the Main Room to witness or hear a portion of the entertainment; or

(d) Who left Ciro's before show time and before the accordion curtain was opened.

The plaintiff does not contend that the facts found in paragraph XXII are not true, only that the finding is "irrelevant." However, since the facts are true and are supported by the evidence and stipulations, the defendant is entitled to such a finding insofar as it has a bearing on the conclusions of law the Court draws from the evidentiary facts, e.g., paragraph V.

8.

Proposed Finding XXIV. The private groups availing themselves of the facilities of the Pavillion Room had an intent on their part of being assimilated into the general over-all cabaret atmosphere of Ciro's. [155]

The plaintiff's objection to paragraph XXIV is not well taken. Paragraph XXIV is based upon the Court's Opinion. On page 16 the Court said:

> "* * * Under such circumstances I find that the private groups availing themselves of the facilities of the Pavillion Room did not consider themselves as part of the public patronage at Ciro's and that any intent on their part of being assimilated into the general over-all cabaret atmosphere of Ciro's was of incidental sig-

nificance in their decision to conduct their parties in the Pavillion Room."

The Court does find in that paragraph in its Opinion that there was an intent on the part of the patrons of being assimilated into the general overall cabaret atmosphere of Ciro's and properly, in the following paragraph, the Government proposes in the words of the Court that said intent was of "incidental significance." Therefore, both paragraphs XXIV and XXV objected to in plaintiff's paragraphs 8 and 9 are based on the words and findings of the Court and the preponderance of the evidence.

9.

Proposed Finding XXV. Said intent was of incidental significance in their decision to conduct their parties in the Pavillion Room.

Finding of Fact XXV is correct and based on the language of the Court. See discussion in preceding paragraph 8.

10.

Proposed Finding XXIX. Plaintiff has not established the time when payment was actually made by or for the patrons or guests of the Pavillion Room on any of the 304 occasions, for any of the following: [156]

(a) The food served;
(b) The drinks served before dinner; or
(c) The drinks served during dinner.

The plaintiff has established that the drinks served after dinner and after the commencement of

show time were paid for at that time, and the cabaret tax applicable thereto was $5,200.63.

Again, the plaintiff does not dispute the truth of the facts found in paragraph XXIX. The plaintiff seeks the omission of the paragraph only on the ground that the finding is irrelevant. It is suggested that the facts being true, they should be found, and that plaintiff's objection should be not to the appropriateness of the finding of fact but if anything, he instead should suggest an appropriate conclusion of law. In view of paragraph V of the conclusions of law, it is submitted that an appropriate conclusion of law has already been submitted. The second sentence of finding XXIX must be found by the Court or else there is not a sufficient factual basis for the judgment the Court has granted the defendant on its counterclaim.

11.

Proposed Finding XXXIII. The plaintiff held out to the prospective organizations desiring to use the Ciroette Room the promise of seeing the entertainment at 10:30 p.m. Some 5% of the Ciroette patrons did in fact avail themselves of this opportunity. The Government assessed a cabaret tax based on 5% of the receipts taken in by the Ciroette Room.

The apparent objection of the plaintiff to Finding XXXIII is that it is not expressed in the narrow terms of the written Stipulation of Facts. However, plaintiff concedes that the Court did use the lan-

guage of paragraph XXXIII in its Opinion, page 19. The facts are clear that the promise of seeing the entertainment at 10:30 p.m. was held out to at least 5% of [157] the Ciroette Room patrons and at least 5% of them did avail themselves of the opportunity. Therefore, the finding is true and should be made. As the Court said on page 19 of its Opinion: "The nature of the private parties being similar to those being conducted in the Pavillion Room and the prior discussion on the subject is pertinent" to the Ciroette Room. Therefore, as in the Opinion, where a reference is made to the discussion of the Pavillion Room and is incorporated later, so in the findings, a similar finding with respect to the Ciroette Room should be made as was done with the Pavillion Room. The essence of the finding relating to the Pavillion Room is found in paragraph IX.

12.

Proposed Finding XXXVII. On the "Closed House" occasions, the show and orchestras usually provided were the same as was regularly staged by Ciro's and Ciro's advised the private organizations as to the amount and distribution of the payments to be made to the performers if the private organizations should hire them. On none of the 20 occasions in issue did the representatives of the private organizations directly deal with the entertainers or their theatrical agents; instead, they dealt through Ciro's personnel, agreeing to pay for the music and entertainment the price Ciro's personnel fixed. In addition to the 20 occasions in issue, during the

period involved in this lawsuit there were some 14 other occasions in which private organizations held "Closed House" parties at Ciro's in which representatives of the organization either negotiated directly with Ciro's entertainers or other entertainers, which occasions the defendant did not treat as taxable.

Plaintiff states that "the first part" of Finding XXXVII is contrary to the facts contained in the Opinion. Plaintiff fails to state wherein the facts are contrary. Plaintiff did not state wherein the findings were contrary because [158] they aren't and he cannot. For instance, the first sentence of proposed Finding XXXVII reads as follows: "On the 'Closed House' occasions, the show and orchestras usually provided were the same as was regularly staged by Ciro's and Ciro's advised the private organizations as to the amount and distribution of the payments to be made to the performers if the private organizations should hire them." The Court actually said at Opinion, page 22: "I attach little significance to the fact that the show usually provided was the same as that regularly staged by Ciro's and that Ciro's advised the private organizations as to the amount and distribution of the payments to be made to the performers if the private organizations should hire them." [Emphasis supplied.] Plaintiff cannot, therefore, be heard to object that the first sentence is not a fact. He may have wished to add or suggest a conclusion of law that said fact is not of great significance, but the fact was found by the Court and remains a fact.

The second sentence is based on the evidentiary facts and is not contrary to the Court's discussion on page 22 of the Opinion; it is the finding that supports the conclusions of the Court on page 22: "It appears, that at best, Ciro's was acting as an intermediary for the convenience of the private groups." The evidence is clear with respect to the twenty occasions in issue, the representatives of the private organizations did not deal directly with the entertainers or theatrical agents but through Ciro's and its personnel.

The final sentence of the proposed finding relates to the fourteen other occasions, in which the Government determined that "Closed House" parties were truly not public performances for profit because they adhered to the criteria set forth in Treasury Rulings. It is submitted that said finding is true, material and relevant to the issues posed by the pleadings. The sentence is based upon the stipulation made in open court with [159] respect to the testimony of Chester Ross, Internal Revenue Agent.

13.

Proposed Finding XXXVIII. In all checks in payment were made payable by the private groups to the performers. Private groups could if they so desired rent the Main Room without the Ciro entertainment and could furnish instead their own entertainment and orchestra. On none of the twenty occasions in issue did they do so. Indeed, when the Ciro entertainers were retained by the private

groups they were able to exercise control over the time when the performers would commence and the type of performance. Any service rendered by Ciro's was purely advisory and for the convenience of the private group.

Plaintiff wishes to omit from paragraph XXXVIII the sentence: "On none of the twenty occasions in issue did they do so." That is, did the private groups rent the Main Room without the Ciro entertainment and furnished instead their own entertainment and orchestra? As support for his denial of the truth of this fact, plaintiff states that he testified "that the private groups generally had special entertainment to suit the occasion." It is submitted that Mr. Hover's testimony should be taken with more than a grain of salt because of his complete lapse of memory with respect to particular occasions. The testimony of the impartial witnesses and the exhibits in evidence clearly show that on the twenty occasions in issue the regular Ciro's entertainment and orchestra were used. This is further reason for the inclusion of the disputed last sentence in paragraph XXXVII based on Mr. Ross' testimony.

The Court will note that no reference has been made to any reporter's transcript. The defendant has been attempting to secure the reporter's transcript ever since the time of the trial. One of the reporters, who took down the first day's testimony, has been in and out of the hospital and has been unable to complete it. [160] It is hoped that the

Court will defer action on any motions for a new trial until we have an opportunity to secure the reporter's transcript, which we hope to have within the next week.

14.

Proposed Finding XXXIX. Ciro's did not furnish the entertainment on these twenty evenings in issue. The private organizations remained free to reject the regular entertainment appearing at Ciro's and if they chose to engage such performers, could modify their acts to suit their own purposes. In none of the twenty instances in issue did they reject the regular entertainment.

In finding XXXIX, the plaintiff likewise objects to the sentence: "In none of the twenty instances in issue did they reject the regular entertainment." The finding is true and material and relevant to the issues presented for the same reasons expressed in our paragraph 13.

15.

Proposed Finding XL. Although on 6 of the 20 nights in question, the public was admitted, the public was admitted only after the private groups had concluded their private parties and surrendered the premises. The public then witnessed the same entertainment that had been paid for by checks of the private organizations to the management of Ciro's and enjoyed the same entertainment, which in each of the six instances in issue was the same entertainment regularly provided by Ciro's during the period involved.

The plaintiff objects to the second sentence of paragraph XL, stating: "There is no competent evidence to establish what entertainment was given in the 6 instances referred to." The record is replete with evidence that on the 20 occasions in issue the same entertainers and orchestras regularly playing at Ciro's were booked into Ciro's for those evenings. The issue [161] always has been and was throughout the trial only whether this entertainment was furnished by Ciro's or by the private organizations. The question has been who provided the entertainment, not that this wasn't the same entertainment as was regularly booked into Ciro's. The evidence is clear that the regular entertainment did perform on the twenty nights in question. Likewise, the evidence is clear that Ciro's itself did not pay for this entertainment on the six evenings in question but that the payment was made by separate checks made by the organizations. See Finding XXXVIII, above. The evidence is further clear that on the six evenings in question the general public was admitted to Ciro's after the private groups had concluded their parties. Of course, entertainment and floor shows were provided on those evenings and there is certainly a reasonable inference that it was the same orchestras and entertainment that had there performed for the private organizations.

16.

Proposed Conclusion I. The statute imposing the cabaret tax is not intended to cover those pre-performance parties by those patrons whose desire to

be present at the public performance was incidental to some more cogent reason for attending the cabaret performance, such as a gathering of a private group or organization for the conduct of its business.

The plaintiff objects to the word "performance" after the word "cabaret" in the Conclusion I. Defendant was attempting to clarify the conclusion in terms of the statute [I.R.C. 1939, Sec. 1700 (e) (1)] in that defendant's interpretation was that it was the attendance at the performance in the cabaret that was the critical fact giving rise to taxability, not mere attendance in a cabaret.

17.

Proposed Conclusion III. The criteria of taxability is [162] not whether the amounts paid by or for patrons of the Pavillion Room for food, refreshment and merchandise entitled them to be present during a portion of a public performance for profit or whether the parties when viewed in their entirety are public or private but whether the motive of the private groups engaging the private room was other than to be present at the entertainment.

Plaintiff desires to omit Conclusion III because it "does not appear to completely state the conclusion set forth in the Opinion." The plaintiff fails to submit a proposed conclusion which he believes completely states the conclusion. The particular language of the Opinion is found on page 11, as follows: "Even assuming arguendo that in view of

the removal of the partition at or about 10:30 p.m. there was a public performance in regard to the Pavillion Room guests it is not determinative of whether such guests were entitled to be present under the meaning which I have ascribed to such words. The fact that the Pavillion Room parties may have been public when viewed in their entirety is immaterial insofar as it pertains to the pre-performance receipts if it be shown that the main purpose of private groups in engaging the Pavillion Room was other than to be present at the entertainment." It is submitted that Conclusion No. III is a correct paraphrase of the discussion of the Court in such a form that it makes a coherent and concise conclusion of law.

Conclusion

For the foregoing reasons, it is respectfully submitted that the proposed Findings of Fact, Conclusions of Law and Judgment should be executed as proposed.

Respectfully submitted,

LAUGHLIN E. WATERS,
United States Atty.;

EDWARD R. McHALE,
Asst. U. S. Atty., Chief, Tax Division;

/s/ EDWARD R. McHALE,
Attorneys for Defendant.

[Endorsed]: Filed February 21, 1958. [163]

[Title of District Court and Cause.]

MOTION FOR NEW TRIAL, AND MOTION TO AMEND AND MAKE ADDITIONAL FINDINGS OF FACT AND CONCLUSIONS OF LAW

(Fed. R. Civ. P. §§ 52 & 59)

Defendant, United States of America, through its counsel of record, moves the Court for an order vacating and setting aside the judgment dated February 25, 1958, and filed and entered February 28, 1958, and for a new and further trial, or for judgment in favor of the defendant as prayed for in the defendant's answer and counterclaim, and to amend the findings of fact and conclusions of law and to make new findings and conclusions.

Defendant bases its motion for new trial on the same grounds and the same papers set forth in its motion for new trial heretofore filed on January 13, 1958, with respect to the decision filed and entered January 3, 1958, and incorporates said motion herein by reference as if set forth again in full.

In addition, it is urged that the Court erred in its conclusions of law I, II, III, V, VI, and VII, as being erroneous [165] conclusions and based on insufficient evidence.

Motion to Amend and Make Additional Findings of Fact and Conclusions of Law

Defendant has heretofore, on February 14, 1958, lodged with the Clerk proposed findings of fact

and conclusions of law, which the Court has considered and adopted in part and rejected in part. With respect to said findings of fact which have been omitted by the Court from its findings executed February 25, 1958, it is submitted that the findings should be amended to add the following:

Proposed finding XX;
Proposed finding XXI;
Proposed finding XXII;
Proposed finding XIV;
Proposed finding XV;
Proposed finding XVI; and

the words "and entertainment" omitted from Proposed finding XIX;

Proposed finding XXIX;

the failure to find all but the first sentence of Proposed finding XXXVII; and

the failure to find the third sentence of Proposed finding XXXVIII, to wit, that on none of the 20 occasions in issue did representatives of private organizations deal directly with the entertainers or their theatrical agents and on none of those occasions did they furnish their own entertainment and orchestra or reject the regular entertainment appearing at Ciro's; and

the last sentence of Proposed finding XL. [166]

The foregoing proposed amendments to the findings of fact are based upon the evidence and are for the reasons set forth in Defendant's Reply to Ob-

jections to Proposed Findings of Fact and Conclusions of Law, filed February 21, 1958, which is incorporated herein by reference.

Respectfully submitted,

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant United States Attorney, Chief, Tax Division;

/s/ EDWARD R. McHALE,
Attorneys for Defendant,
United States of America.

Affidavit of Service by Mail attached.

[Endorsed]: Filed March 10, 1958. [167]

United States District Court for the Southern District of California, Central Division

No. 20853—WM Civil

HERBERT D. HOVER, d/b/a CIRO'S,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

FINDINGS OF FACT, CONCLUSIONS OF LAW AND JUDGMENT

The above cause came on regularly for trial on December 19, 1957, before the Honorable Irving R.

Kaufman, United States District Judge, presiding, without the intervention of a jury, the plaintiff represented by his attorney, Ernest R. Mortenson, Esq., the defendant represented by its attorneys, Laughlin E. Waters, United States Attorney, and Edward R. McHale, Assistant United States Attorney, Chief, Tax Division; and after having been continued for further [170] trial from time to time, and evidence received, briefs filed, and oral arguments having been heard, and having on December 26, 1957, been duly submitted, and the Court having duly considered the evidence, briefs and arguments of the parties, and having on January 3, 1958, filed its opinion, now finds as follows:

Findings of Fact

I.

On November 14, 1955, the authorized delegate of the Secretary of the Treasury assessed against Herbert D. Hover, d/b/a Ciro's, cabaret taxes for the period June 1, 1951, through March 31, 1955, in the sum of Sixty-seven Thousand Six Hundred Sixty Dollars and Sixty-two cents ($67,660.62) taxes and Seven Thousand Eight Hundred Fifty-eight Dollars and Fifty-one cents ($7,858.51) interest, for a total assessment of Seventy-five Thousand Five Hundred Nineteen Dollars and Thirteen cents ($75,519.13). Notice and demand for payment of the said taxes and interest was made upon the plaintiff on November 16, 1955, and he paid the sum of Three Hundred Dollars ($300.00), and no more, on Au-

gust 7, 1956, leaving an outstanding balance of said assessment of Seventy-five Thousand Two Hundred Nineteen Dollars and Thirteen cents ($75,219.13), together with interest as provided by law.

II.

The aforesaid deficiency assessment of [171] cabaret taxes represented additional taxes assessed with respect to three phases of plaintiff's operation for the period involved: The Ciroette Room; the Pavillion Room and the "Closed House" parties. Of the total assessment of Sixty-seven Thousand Six Hundred Sixty Dollars and Sixty-two cents ($67,660.62), Nine Hundred Ninety-two Dollars ($992.00) is attributable to "Main Room operations" and is conceded to be due and owing by the plaintiff because of a clerical error and is not in issue in this lawsuit.

III.

The amounts of the respective deficiencies in tax determined by the Revenue Agents who made the audit, was based on their examination of plaintiff's books and records and applied the cabaret tax to a certain percentage of the receipts of each room on a basis that is more fully detailed hereinafter. The taxpayer did not consider the receipts here in issue of the said rooms taxable and, consequently did not, in his books and records, segregate any portion of the receipts as Federal cabaret taxes.

IV.

Plaintiff maintained records showing receipts and the computation of the cabaret tax as reported on

the tax returns, but plaintiff kept no records showing what, if any, proportion of the persons who attended the parties in the Pavillion Room stayed for the floor show or for dancing. [172]

V.

Ciro's, located on Sunset Boulevard in Los Angeles, is subdivided into three rooms in which the services and facilities of the Club are offered to the public. In addition to the main entertainment and dining room, herein referred to as the "Main Room," there are the "Pavillion" and "Ciroette" rooms. A lounge or cocktail bar located adjacent to the Main Room also serviced Ciro's patrons but its operations are not involved in this suit. In issue in this proceeding are the taxability of receipts from (1) the Pavillion Room, (2) the Ciroette Room and (3) the "Closed House parties"—when the entire club was closed to the public and reserved for the exclusive use of private organizations.

VI.

The Pavillion Room is located adjacent to the lounge (which is basically a raised extension of the Main Room) and is separated therefrom by a movable wall and thick, soundproof curtain. This room was used primarily to accommodate private organizations which desired to reserve for the evening such a room for the exclusive use of its members.

VII.

The Government assessed a cabaret tax on 94% of the receipts attributed to 304 private parties con-

ducted in the Pavillion Room. The 6% of the receipts excluded from the tax represents amounts paid for food, refreshment or merchandise by or for patrons or guests who are presumed to have left prior to seeing the floor show. [173]

VIII.

While there is some variation in the way these 304 parties were conducted, for the most part private organizations would contact Ciro's for the purpose of arranging for the use of the Pavillion Room on a particular night for the exclusive use of its members. A contract would be negotiated and a deposit secured. Generally dinner would be served commencing some time around 7:00 p.m. and terminating before 10:30 p.m. During this period the movable partition separating the Main Room from the Pavillion Room would remain closed and the parties had the complete and uninterrupted privacy of the Pavillion Room to do as they pleased. Depending on the nature of the organization, speeches, awards, community singing, local entertainment or dancing to music either piped in from the Main Room or furnished by their own hired orchestra might follow the dinner. In any event at approximately 10:30 p.m. the separation was usually removed so as to enable the groups to view the floor show in the Main Room.

IX.

The patrons attending the dinner in the Pavillion Room expected to be able to see the entertainment

in the Main Room, it being the understanding, whether committed to writing or not, that the so-called private parties would be afforded this privilege. Upon conclusion of the floor show, most of the guests at the private parties left the [174] premises.

X.

In view of the removal of the partition at or about 10:30 p.m., there was a public performance in regard to the Pavillion Room guests from that time on.

XI.

The 304 parties in dispute were private up to 10:30 p.m.

XII.

Ciro's was a famous night club which widely advertised its entertainment.

XIII.

In its advertising Ciro's offered the facilities of the Ciroette Room and the Pavillion Room to banquet groups. One of the several inducements for arranging such gatherings in these rooms was the opportunity to view the floor show.

XIV.

The floor plan and structural layout of the Main Room and the Pavillion Room compels the finding that two separate and distinct rooms were contemplated by Mr. Hover and that it was intended that Ciro's would acquire the private party business by offering the privacy necessary to these organiza-

tions in the execution of their customary meetings or gatherings while affording them the opportunity of functioning in a well-known establishment like Ciro's. [175]

XV.

The two rooms are separated by a lounge with separate seating and dining facilities. The lounge is a slightly elevated portion of the Main Room and the Pavillion Room is further raised, thereby creating a six-step elevation differential between the Pavillion Room and the Main Room. Because of this added height the patrons sitting in the Pavillion Room can view the entertainment in the Main Room when the separation wall and curtain are withdrawn by looking through the adjacent lounge. Since the stage is located at the other end of the Main Room, obtaining a good perspective of the floor show from all portions of the Pavillion Room is difficult in view of the distance involved, and those in the rear of the Pavillion Room must move their seats into the fore part of that room in order to view the show. Though ingress and egress to both rooms is possible by way of the lounge, the Pavillion Room has in addition its own separate entrance. Rest Rooms are shared in common with the Main Room, though entrance can be made from the Pavillion Room itself. Each room has its separate dance floor and band stand. Tables and chairs used in the respective rooms seem to be of a different character and their arrangement dissimilar. The building plans further disclose that the two rooms were not constructed as one unit but that the Pavil-

lion Room was added long after the Main Room had been in existence. Upon the closing of [176] the partition separating the two rooms there is an atmosphere in the Pavillion Room of complete privacy.

XVI.

This privacy together with the facilities available at Ciro's was found attractive by the private organizations.

XVII.

A comparison of the respective operations of both rooms further discloses an intent on the part of the management to treat the rooms other than as a single unit. There are some 25 basic differences in the operations of the two rooms. To mention but a few such distinctions—there were differences in menus, prices, services, working hours and duties of the waiters, manner of payment, parking fees, cover charges, etc.

XVIII.

It is clear from the evidence presented that the serving of food in the Pavillion Room was completed before the beginning of the floor show.

XIX.

Any intent by the private organizations of being assimilated into the general over-all cabaret atmosphere of Ciro's was of incidental significance in their decision to conduct their parties in the Pavillion Room.

XX.

Said groups did not consider themselves as part of the public patronage at Ciro's. [177]

XXI.

Their conscious choice to reserve the Pavillion Room which was located at considerable distance from the main sphere of activity indicates that the prime moving consideration in selecting the Pavillion Room was the desire to achieve some sense of privacy for their group activity and business—at least until the entertainment began.

XXII.

Upon the removal of the partition at show time, the Pavillion Room guests did observe and participate in the public performance in common with the other patrons in the Main Room and no distinction between the two rooms is warranted during this period. The position of the Pavillion Room guests during this period is analogous to the patrons of the lounge during the show or to the late-comers to the Main Room, who because of the crowded conditions existent there, are forced to stand at the bar in the lounge in order to see the floor show. Any payments from drinks or refreshments made by these patrons were, of course, subject to the tax.

XXIII.

With respect to the $55,581.98 assessed against the Pavillion Room receipts, the parties have stipu-

lated that $5,200.63 would represent the tax on food, refreshment or merchandise served to patrons or guests subsequent to 10:30 p.m. [178]

XXIV.

No admission charge was made to enter the Main Room from either the Ciroette Room or the Pavillion Room.

XXV.

The Ciroette Room like the Pavillion Room was used primarily to accommodate private gatherings. However, unlike the Pavillion Room, it was located on the second floor of the building and those patrons desiring to see the floor show could do so only by descending a flight of stairs and passing through two doorways to the Main Room.

XXVI.

The plaintiff permitted members of private organizations using the Ciroette Room to see the entertainment at 10:30 p.m. Some 5% of the Ciroette patrons did in fact avail themselves of this opportunity. The Government assessed a cabaret tax based on 5% of the receipts taken in by the Ciroette Room.

XXVII.

It was stipulated that if any tax is due it is to be computed on the basis of 5% of these receipts and the only question presented for consideration is whether as a matter of law the cabaret tax applies to this 5%.

XXVIII.

The nature of these private parties being similar to those conducted in the Pavillion Room, the prior findings [179] on this subject are pertinent here and incorporated by reference. However, the reasons for denying the tax on pre-performance receipts in the Pavillion Room are even more potent here in view of the obvious remoteness of the Ciroette Room and the substantial effort and distance to be traversed for its patrons to observe the floor show.

XXIX.

Part of the initial deficiency assessment consists of a 20% tax on all amounts paid for admission, refreshment, service or merchandise on twenty evenings when all the facilities of Ciro's were reserved by and for the members of one particular organization, referred to for convenience as "Closed House" parties.

XXX.

On the "Closed House" occasions, the show and orchestras usually provided were the same as was regularly staged by Ciro's and Ciro's advised the private organizations as to the amount and distribution of the payments to be made to the performers if the private organizations should hire them.

XXXI.

The private organizations themselves contracted for the entertainment and music supplied to the "Closed House" parties. In all cases checks in pay-

ment were made payable by the private groups to the performers. Private groups [180] could, if they so desired, rent the Main Room without the Ciro entertainment and could furnish instead their own entertainment and orchestra. Indeed, when the Ciro entertainers were retained by the private groups they were able to exercise control over the time when the performers would commence and the type of performance. Any service rendered by Ciro's was purely advisory and for the convenience of the private group.

XXXII.

Ciro's did not furnish the entertainment on these twenty evenings in issue. The private organizations remained free to reject the regular entertainment appearing at Ciro's and if they chose to engage such performers, could modify their acts to suit their own purposes.

XXXIII.

Although on 6 of the 20 nights in question, the public was admitted, the public was admitted only after the private groups had concluded their private parties and surrendered the premises.

Conclusions of Law

And from these facts the Court concludes as follows:

I.

The statute imposing the cabaret tax is not intended to cover those pre-performance parties by

those [181] patrons whose desire to be present at the public performance was incidental to some more cogent reason for attending the cabaret, such as a private gathering of a private group or organization for the conduct of its business.

II.

The words "entitled to be present" in the statute do not apply to the Pavillion Room or Ciroette Room parties where the main purpose of the parties engaging such rooms was other than to be present at the entertainment.

III.

If the parties had ended before the commencement of the floor show or if the partition had remained closed and the Pavillion Room patrons excluded from entering the Main Room or observing the entertainment therein, the expenditures before 10:30 p.m. would not lie within the scope of the tax, even if the group using the Pavillion Room had arranged for their own entertainment, since under the statute there would be no public performance.

IV.

It has been stipulated that the $5,200.63 representing the tax on drinks served after 10:30 p.m. is equivalent to the tax on the amounts paid for food, refreshment, and merchandise by or for patrons or guests of the Pavillion Room entitled to be present during such performance for profit and is the cor-

rect amount of tax on the Pavillion [182] Room operation. The Court concludes that of the amount assessed against the plaintiff with respect to the Pavillion Room, the amount representing the service of drinks after 10:30 p.m., in the sum of $5,200.63, is the proper tax on amounts paid by or for patrons or guests in the Pavillion Room for food, refreshment or merchandise after 10:30 p.m.

V.

The tax assessment on 5% of the Ciroette Room's receipts is improper.

VI.

After the private groups had concluded their parties and surrendered the premises, the club subsequently reverted to a cabaret status and this has no bearing on the nature of the parties from which the public was rigidly excluded.

VII.

With respect to the "Closed House" parties, the payments received by Ciro's did not entitle the patrons or guests to be present during public performances for profit.

VIII.

Defendant is entitled to judgment on its counterclaim for the tax on the amounts paid for refreshment in the Pavillion Room after 10:30 p.m. and for its costs. [183]

Judgment

In accordance with the foregoing findings of fact and conclusions of law, It Is Ordered, Adjudged and Decreed:

(1) That plaintiff take nothing by his complaint for refund of $300.00, and that it be dismissed with prejudice;

(2) That defendant have judgment against plaintiff on its counterclaim for the sum of $7,463.86, together with interest on this judgment until paid according to the law and for costs to be taxed by the Clerk of the Court.

Costs taxed—$111.96.

Dated: This 25th day of February, 1958.

/s/ IRVING R. KAUFMAN,
United States District Judge.

[Endorsed]: Filed and entered February 28, 1958. [184]

United States District Court
Chambers of
Judge Irving R. Kaufman
United States Courthouse
New York 7, N. Y.

March 13, 1958

In re: Herbert D. Hover, dba Ciro's vs. United States of America No. 20853-WM-Civil—Southern District of California, Central Division

Edward R. McHale, Esq.,
Assistant U.S. Attorney,
Southern District of California
808 Federal Building
Los Angeles 12, California

Dear Mr. McHale:

I have considered your Motions for a New Trial and to Amend and Make Additional Findings of Fact and Conclusions of Law in the above entitled action.

I am familiar with your contentions and do not feel that they warrant the granting of either motion. Nor do I feel that oral or written argument is necessary in this case. I am accordingly denying the motions in all respects.

I am forwarding a copy of this letter to the Clerk of the United States District Court, Southern District of California, with the instruction that he make the necessary notation on the motion papers.

Sincerely yours,

/s/ IRVING R. KAUFMAN.

CC: Ernest R. Mortenson, Esq.
961 East Green Street
Pasadena, California

John A. Childress, Esq.
Clerk, U.S. District Court
Southern District of California
U.S. Post Office & Courthouse Bldg.
Los Angeles 12, California

[Endorsed]: Filed March 17, 1958. [184-A]

[Title of District Court and Cause.]

ORDER DENYING MOTIONS FOR NEW TRIAL AND MOTION TO AMEND AND MAKE ADDITIONAL FINDINGS OF FACT AND CONCLUSIONS OF LAW

The defendant having heretofore filed on January 13, 1958, a motion for new trial under Rule 59, and having on March 10, 1958, filed a motion for new trial under Rule 59 and motion to amend and make additional findings of fact and conclusions of law under Rule 52(b), and the Court having duly considered the same and the papers in support thereof and in opposition thereto, now, therefore,

It Is Hereby Ordered that defendant's Motion for New Trial filed January 13, 1958, and its Motion for

New Trial and Motion to Amend and Make Additional Findings of Fact and Conclusions of Law filed March 10, 1958, are denied.

Dated: March 28, 1958.

/s/ IRVING R. KAUFMAN,
United States District Judge.

Approved as to Form, pursuant to Local Rule 7(a), this 25th day of March, 1958.

/s/ ERNEST R. MORTENSON,
Attorney for Plaintiff.

[Endorsed]: Filed March 31, 1958. [186]

[Title of District Court and Cause.]

NOTICE OF APPEALS

To the Above-Named Plaintiff, Herbert D. Hover, dba Ciro's, and His Attorney, Ernest R. Mortenson, 961 East Green Street, Pasadena, California:

You, and Each of You, Are Hereby Notified that the United States of America, defendant and counterclaimant above named, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the following judgments:

(1) From the judgment entered January 3, 1958, in favor of plaintiff as to which a Motion for New

Trial filed January 13, 1958, was ordered denied by orders entered March 17 and March 31, 1958; and from the entry of said orders of denial.

(2) From the judgment entered February 28, 1958, in favor of plaintiffs as to which Motions for a New Trial and to Amend and Make Additional Findings of Fact and Conclusions of Law [188] filed March 10, 1958, were ordered denied by orders entered March 17 and March 31, 1958; and from the entry of said orders of denial.

Dated: May 13, 1958.

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant United States Attorney, Chief, Tax Division,

/s/ EDWARD R. McHALE,
Attorneys for Defendant,
United States of America.

Affidavit of service by mail attached.

[Endorsed]: Filed May 14, 1958. [189]

In the United States District Court, Southern District of California, Central Division

No. 20,853—WM Civil

HERBERT D. HOVER, dba, CIRO'S,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

Honorable Irving Kaufman, Judge Presiding.

REPORTER'S TRANSCRIPT OF PROCEEDINGS

Thursday, December 19, 1957

Appearances:

For the Plaintiff:
ERNEST R. MORTENSON, Esq.

For the Defendant:
LAUGHLIN E. WATERS,
United States Attorney; by
EDWARD R. McHALE,
Assistant United States Attorney.

The Court: You may proceed.

The Clerk: 20,853-WM Civil, Herbert D. Hover doing business as Ciro's, vs. United States of America for trial.

Mr. Mortenson: Ready for the plaintiff, your Honor.

Mr. McHale: Ready for the Government.

The Clerk: Your Honor, I think the record should show that Exhibits 1, 2, 3-A, 3-B, 3-C and 3-D; 4-A, 4-B and 4-C have been marked for identification.

The Court: Very well. I would like to have an opening statement, gentlemen.

Mr. Mortenson: Very well, your Honor.

If your Honor please, since the physical set up of the plaintiff's establishment is important I would like to start with a short description of the layout of the room.

I know your Honor is familiar with the briefs filed and with the pleadings, so I shall not waste any time on the basic issues which have been set forth.

Ciro's, is, I am sure, known to your Honor. It is not only known as a night club on the West Coast but is well known throughout the United States.

It is located on what we call the "Sunset Strip."

The downstairs I might describe by using this courtroom. The main room contains a place for the orchestra and the [3*] usual tables and chairs. You might say that the main room then would be the area from here back with the orchestra in the same position that the judge occupies.

Then there are three steps that go up to a lounge. If the lounge starts here we would say the lounge would go back to the railing.

***Page numbering appearing at top of page of original Reporter's Transcript of Record.**

Now originally that was all that constituted the building. Then in 1951 Mr. Hover built another building contiguous to this one. That is where the Pavillion Room is located which is the subject of one issue in the case. The new building would constitute this area where the benches are located.

Now, where the railing stands there is a base about the height of this railing—a solid base going across the full length of the room with a door in the center of the railing and there are two steps just in front of that.

Now, above the railing there is constructed a movable accordion wall. It is soundproof. And it goes to the ceiling.

When the wall is closed and the two sides come completely together no one sitting in the Pavillion Room can see anything in the main room nor can anything be heard in the main room.

In addition to this accordion wall there is a curtain, a three-ply fabric which is an additional soundproofing [4] device. That is usually closed in addition to the wall when we speak about the accordion wall being closed.

One of the issues in the case revolves around the Pavillion Room. The agents have set up a tax on the receipts from 304 private parties held in the Pavillion Room.

Now, the usual arrangement was this. Perhaps an example would illustrate it best. Supppose the Sigma Chi's were going to have their annual party. They figured on an attendance of 100. The chairman of the Sigma Chi dinner committee would call Ciro's

and would ask what the cost would be for a party of 100 at Ciro's.

They would be told that the Pavillion Room was available; that the wall would be closed between the Pavillion Room and the main room and that with a certain menu the dinner would cost $6 each for the 100 people or $600, including tips and including the local three per cent sales tax.

In some instances, or perhaps in most instances as we will learn later, this amount would be broken down into say $5 for the meal and an additional amount for the tip and an additional amount for taxes. But the point is that in each instance an agreement was made and that was followed up by a letter which was sent to the chairman who returned one copy of the letter.

These dinners usually began around 6:30 or 7:00 o'clock. The group would come in through a separate entrance. The [5] Pavillion Room has its own entrance from the street.

There is one entrance from the Pavillion Room into the ladies' room on that floor and likewise one entrance from the men's room—from the Pavillion Room into the men's room on that floor.

There is another entrance into the same men's room from the main—well, it is really from the lounge and there is an entrance from the lounge into the ladies room.

A typical party there would be a dinner served and speeches heard. And then in some of the parties the wall would be moved open, say around 10:00 o'clock, so that those who remained at the party

could see the floor show which was currently being shown in the main room at Ciro's.

The Court: Mr. Mortenson, was there any representation made in advance of the renting of the Pavillion Room, as an inducement to renting it, that such would be the case—that these sliding doors would be opened?

Mr. Mortenson: In some cases the ones who arranged the party were told that they could remain and see the floor show, yes.

The Court: You say in some cases. Generally—I take it this will be developed during the case, but generally I take it that Ciro's does extensive advertising. I come from New York and we hear of Ciro's in New York.

The query is: As part of this advertising and the renting [6] of the facilities must be in response to this advertising. Did they hold out this inducement that the entertainment would be available?

Mr. Mortenson: In many of the advertisements it was stated that they could stay for the floor show, yes, and that will be more fully developed as Mr. Hover takes the stand because it isn't quite as easy or as simple an issue as it appears.

The Court: I understand that.

Mr. Mortenson: But that did appear in the ads—that they could stay for the floor show.

Now, the operation of a restaurant and night club business is intricate like many things in life and I have learned a lot since I got into this case about the various problems and the different techniques that

are involved with respect to private parties and the regular main room operation.

That will be filled in in detail when Mr. Hover testifies, but briefly I would like to mention this just as a frame of reference.

In the Pavilion Room there was a different menu from the one in the main room. The portions were smaller because the price was less.

There we have a table d'hote situation where it is a la carte in the main room. If they have steak, for instance, it is a 14-ounce steak in the main room where you would have [7] a 12-ounce steak in the Pavilion Room. The menu was different and the waiter situation basically is this.

The union has a completely different scale and different rules for banquet waiters from regular waiters. For instance, in the Pavilion Room a waiter could serve no more than 20 people. In the main room a waiter had a particular station and he would have to serve any number of people at the tables where he had to give his service.

The Court: When I inject and ask questions I don't want you to assume from that that I have an opinion because I don't. I am just searching for information.

Mr. Mortenson: I know what a judge means by his questions. I understand that.

The Court: Frequently lawyers, you know, are deceived in believing by the questions the judge asks indicates his thinking. There is nothing more wrong than that.

Now, why do you emphasize this point with re-

spect to the fact that a waiter could only have 20 people to wait on in the Pavilion Room and it is unlimited in the main room? What is your point there?

Mr. Mortenson: I hate to say I am glad you asked that question, Judge. I am glad you asked it.

One of our basic principles is found in Gear vs. Birmingham (phonetic) and I think it is something like 40 or 45 pages of opinion. [8]

The case involved less than $200 and I remember one judge here remarking, "Well, that judge out there in Alabama," I think it was in Alabama, "must have had a lot of time on his hands." But I don't think that is the point at all.

This section that we are dealing with strangely enough goes all the way back to 1917 when it was passed as emergency legislation for the purpose of getting some money for, I guess, that was World War I, and it has been on the books since.

I don't know of any section that has been massacred more by the legislature than that one. It is a beautiful field for any expert in semantics. He could spend months there finding his way around these words. But there has been quite a lot of judicial development of the law and some of the imaginative writers in the Treasury Department have done wonderful things with regulations that have to do with that section.

Because it is so strangely written, because of the many amendments and because of the commissioner's past experiences in the courts that there is a regulation on almost everything.

Some of them are published. Some of them are letter rules. Some of them are other kinds of rules, but there is a recent ruling and I think the defendant's memorandum refers to it.

It has to do with the character of the operations. If [9] you have one common ownership and you have a taxable entertainment in one room, we will say, and then you have another room where liquor is being served and where food is being served maybe the cabaret tax applies there and maybe it doesn't.

The commissioner has some weird regulations on that that try to tell you when there is tax liability in what they call a "related room."

The Court: Is what you are trying to say to me that one of the elements we must determine is whether these adjunct rooms were part of the operation of the main room?

Mr. Mortenson: Yes.

The Court: And in determining whether it is part of the operation of the main room you then will attempt to show that it was a seperate operation—different waiters, different working hours, different conditions, is that your point?

Mr. Mortenson: That is right, your Honor, because the Government, I am sure, is going to take that position and in anticipation of that I would just like to fit that in. That is it. In other words, they are going to say, "Well, this falls within our related room policy or regulations," or however they want to refer to that.

There are many other differences and I think it

is important to bring that out because you can see that the operation of a banquet room, which is what we have in the [10] Pavilion Room, is something quite different from the operation of an ordinary night club. But that was all I wanted to bring out now that there is an issue there and, of course, our witnesses can do a better job on the details.

The Court: All right.

Mr. Mortenson: Now, as I understand, the Government's position in setting up some $55,000 in taxes on the Pavilion Room, they have the theory that if somebody from this party sees a show then it becomes a public entertainment for profit and incurs the 20 per cent tax.

Now, the plaintiff's position is that this started out as a private party. It ended up as a private party and that any receipts received during that time from the private party are not taxable under this section.

Now, we have a small issue which is pretty much resolved by stipulation with regard to the Ciroette Room.

There is a small room on the second floor of Ciro's which is used entirely for private parties. On occasions after the private party was over some members of the group there would be brought down into the lounge to see the show.

Now, we have stipulated that the number of those was five per cent, so the only issue is whether or not——

The Court: You say the number was five per cent. You mean five per cent of the total charge?

Mr. Mortenson: Yes, sir. The only issue is whether or [11] not there is a cabaret tax applicable when a guest would come from there down to witness the show.

You will permit argument at the conclusion of the case, won't you, your Honor?

The Court: Yes.

Mr. Mortenson: I want to stay away from that as much as possible.

The Court: Yes. As a matter of fact I will welcome it in this kind of case.

Mr. Mortenson: There are some words in the code that are troublesome and perhaps the cause of this whole lawsuit, but I will take that up later. I think it is clear enough if we look at the legislative history and the court decisions as to what law should apply here, with all due respect to my distinguished adversary here, Mr. McHale, who I believe also tried the Naylor case and the La Jolla case which I cited with unfortunate results.

He has a different feeling but, of course, Mr. McHale doesn't choose his cases. They are assigned to him. But the issue of the Ciroette room is basically the same as that of the Pavilion Room.

Now, we have another issue which we call the "Closed house issue."

Now, suppose, to use my Sigma Chi illustration, the next year they had a regional meeting of the alumni and they [12] figured that they would have 400 people there. Then the chairman might call Ciro's and say, "Can we have the whole house for Sunday, January 14," and Ciro's would say, "Yes;

we have nothing else booked" and then the question would come up, "Well, what about an orchestra?"

Well, as will be explained here later, Ciro's had a particular arrangement with one orchestra that was there for quite a period of time. Then what about entertainment? Well, Pearl Bailey is going to start in on Monday, the following Monday. "Maybe we can make arrangements to have her come in Sunday, the day before."

And then the question is, "Well, who is going to make the arrangements?"

So maybe Mr. Hover, if Mr. Hover was there—I don't know whether this is true or not, but I think it will fit the facts in general.

The Court: Mr. Mortenson, would this only occur on occasions such as you point out? In other words, usually in advance of the commencement date of a performer's engagement at Ciro's?

Mr. Mortenson: That varied greatly.

The Court: What would happen in a case, for example, where Pearl Bailey had been playing at Ciro's. It is a seven day a week engagement, isn't it?

Mr. Mortenson: Well now, that—— [13]

The Court: I want to get that clear.

Mr. Mortenson: Yes.

The Court: A seven day a week engagement. Now, what would you do—supposing it happened during the regular engagement week.

Mr. Mortenson: That is something that I have never completely gotten straight in my own mind and I am going to ask Mr. Hover to explain that carefully and in detail.

There were different ways of booking these people and I think in some cases where he had these closed house parties it would be in the midst of a regular engagement. But the rules on this—the variety artist; rules are very strict and you have to fit within those.

Now, we will have that explained. I think it varied according to the entertainer and according to the particular situation at the time. But sometimes the entertainment would be picked up before the regular engagement or after it, and I think sometimes it would be an entertainment that was booked there regularly. But the payment was on a different basis and that was true of the orchestra, too, which will be explained in detail.

When you had a closed house party the payments to the orchestra and the entertainers were usually on a different basis from the regular engagement at Ciro's.

The Court: And if it came during the regular engagement [14] I take it the general public would be barred that night, is that it?

Mr. Mortenson: I don't believe there is any dispute of the fact about that, that the public was not admitted.

The Court: If they came to the door that evening they would be turned away?

Mr. Mortenson: That is right. And usually there was a big sign put up that, Mr. Hover tells me, said "Ciro's closed—go to the Mocambo."

That all sounds very strange to me, that they

would send them to their competitors but that is what they usually did—they went to the Mocambo.

The Court: It seems like the antitrust division will be looking into that.

Mr. Mortenson: The public wouldn't come in because usually it was a ticket affair and somebody who was interested in the money coming in would be right there at the door and keep them out.

Now, I don't believe there has been any dispute of the fact about that. However, on a couple of instances—we have only 20 closed houses involved in this lawsuit.

The closed-house party was over early. And then after everybody left—and I don't believe there is going to be any dispute about that, everybody in the private party left then Ciro's would open up as a nightclub for the remainder [15] of the evening. That happened a couple of times, but I think our closed house issue is basically a problem of interpretation of a regulation which is, as I mentioned in my brief, a rather fantastic presumption and I am going to offer the revenue agent's report sent to Mr. Hover in evidence and that is what was set out in the revenue agent's report—that on the nights when they had closed house parties they treated that as if it was a mere reservation of tables. Those are the words used.

Now, those are the issues here and I think we will develop our facts from the witnesses. Then at the conclusion we could, I think, try to apply the cases to the facts here more intelligently.

Unless you have some questions that is all I have at this time.

The Court: Mr. McHale?

Mr. McHale: We have, if the court please, three issues in this case as Mr. Mortenson has outlined—that is three separate types of rooms or situations that were involved in the tax.

I would like to preface my statement by stating how this case is before the court.

Ciro's, of course, during this period from 1951 to 1955 reported and paid a substantial amount of cabaret tax principally on its main room [16] operations.

In 1955 an audit was made. The agent went out and examined Ciro's and discovered these three situations and determined that a certain amount of tax, additional tax should be assessed and the tax was eventually assessed and there were conferences and claims for abatement but the end result was an assessment of a tax.

Now, Ciro's paid $300 and filed a claim for refund and brought suit.

Because of the financial situation of Ciro's the Government first asserted a jurisdictional defense that he would have to pay all the tax.

Mind you there was just one assessment for all these various periods but we withdrew that and counterclaimed for the entire amount because Ciro's was in Chapter 11 at this time and we felt we should dispose of the whole thing. So, the entire issue is before the court.

Now, it has been conceded and is in the stipula-

tion that there was an arithmetical error by Ciro's and that of the $67,000 they do owe over $900. So, what this really amounts to is a suit by the Government on its assessment. It is not really a refund suit except technically speaking, because the counterclaim is really the thing.

The assessment has been made by the Commissioner. The Commissioner determined this tax is due.

Now, the assessment is made for the period from 1951 to [17] the middle of 1953. The tax would have been payable on a monthly basis and then from that time on it was payable on a quarterly basis but the Commissioner assessed $67,000 with respect to the taxes in dispute—$66,600 some odd dollars.

The Court: Except for nine hundred some odd dollars are we in agreement as to the amount of the assessment?

Mr. Mortenson: Yes.

The Court: Then there is no problem there.

Mr. McHale: They agreed the $992 is due the Government.

The Court: Now, the next agreement I want to have here is the agreement and understanding we made in chambers today, and that was that if eventually the disposition of this case is made upon a breakdown such as of the charges after the entertainment tax—upon charges after the entertainment commenced, that the court will not have to compute the amounts for you gentlemen but that you will, after I have enumerated the proposition by a de-

cision, agree between yourselves as to the amounts that are owing, is that correct?

Mr. Mortenson: Mr. McHale and I are agreed on that.

Mr. McHale: That is correct.

Mr. Mortenson: That we give you such a computation if you require it or if you request it.

The Court: Well, the point is that I am apt to write this opinion after I get back to New York and the chances are [18] I will not be requesting too much after I get back.

Now, I should really, I suppose, in advance ask for this before you complete your case but I was hoping that we could avoid it by a stipulation between yourselves.

Mr. Mortenson: We can agree on a stipulation, I am sure.

Mr. McHale: I am sure we can.

We have a local rule, Rule 7 in this District, which is comparable to the Tax Court Rule 50 which permits the computation. This goes a little beyond. It requires an agreement as to the amounts but I am sure we can agree upon that if your decision is based upon such a premise.

The Court: All right.

Mr. McHale: Now, the agents went into Ciro's and examined the books and records. They determined what the practice had been. In other words they found out that on at least 304 occasions there had been these private parties in the Pavilion Room, and 255 occasions there had been these parties—at least 255 occasions, there have been the

parties in the Ciroette Room and on more than 50 occasions there had been these so-called closed house parties where the entire facilities were taken over by some organization.

The Court: Let me have those figures again. How many occasions was the Pavilion Room?

Mr. McHale: 304 occasions.

The Court: Yes, and the Ciroette Room? [19]

Mr. McHale: 255 occasions.

The Court: And the closed house?

Mr. McHale: I am not sure of the actual amount. It is over 50—between 50 and 55.

The Court: Mr. Mortenson said about 20.

Mr. McHale: 20 are taxable. 20 the Government has assessed the tax against.

The Court: Now, with reference to the Pavilion Room, have the Government assessed against 304 parties?

Mr. McHale: No. This is what the Government has done. The Government went into the Pavilion Room. They looked at the books and records. The books and records didn't show how many parties were held in the Pavilion Room. All they stated was the amount of receipts from the Pavilion Room and they went in—in their examination they examined other records of Ciro's, such as Ciro's reservation file where they made these letter agreements, and they found 304 of those.

They examined those and came to a conclusion after the examination and various investigations, that 96 per cent of the receipts of the Pavilion Room were taxable.

The Court: Will you illustrate during the course of this trial how they arrived at this 96 per cent?

Mr. McHale: Yes, sir.

The Court: Apparently there is no agreement on that. [20]

Mr. Mortenson: Yes; there is as to how they did it. Actually it is 94 per cent.

What they did was to take the percentage of cabaret tax which applied to the main room, and that being 94 per cent, they used that for the Pavilion Room. We are agreed on that.

The Court: You are agreed on that?

Mr. Mortenson: Yes.

Mr. McHale: As to the Ciroette Room they took only five per cent of the proceeds and we have stipulated as to that, so there is no question on the Ciroette Room. In other words, if the tax is due then five per cent of the proceeds are taxable.

The closed house—the agents examined——

The Court: I am curious as to what happened to the other six per cent in the main room.

Mr. McHale: The agents determined that six per cent of the proceeds of the sales of the main room were by people who came in to dine and had a drink and left before the show started.

The Court: All right.

Mr. McHale: Ciro's is the type of nightclub, as the evidence will show, that really doesn't get going until 9:00 o'clock or so and not many people come in before that hour. Most people go there to see the show so that is a small portion of the sales. [21]

The closed house parties, the ones where they re-

served the facilities for one group for most of the evening, the agents found over 50 of those but they didn't say that 50 of those reservations were taxable.

They looked at the criteria which the Commissioner has set forth and determined in those instances in which they used the regular Ciro's floor show and what amounted to a mere reservation of tables, as Mr. Mortenson has noted in his opening statement, on those 20 occasions 100 per cent of those receipts were taxable.

These are just the selected ones that they felt fitted within the criterion. There were many parties, for instance, where a group would bring in their own entertainment—wouldn't use Ciro's, so they made no attempt to tax those.

There were other occasions when they used the entertainment that was playing at Ciro's but they made arrangements themselves with the entertainers. In other words, they went to them and said, "We want you for this evening," but on those occasions when they went to Ciro's and said, "We want to reserve your place for tonight; we want your regular floor show," and Ciro's arranged everything. They may still have paid by check to the entertainers but Ciro's arranged everything and those were the ones that were determined to be taxable 100 per cent.

Now of the 20 there were a few occasions on which there [22] were taxable receipts—the books also show taxable receipts on that night in the restaurant because during that evening the public, in addition

to the people in this party, were admitted and Ciro's considered it taxable. It was only about six out of 20 but I think the agents have found that number where the public—the general public was allowed to come in.

One further thing with respect to these closed-house parties.

The people who would attend these parties—some group would arrange for the party. It might be a community charitable organization or a working group of some kind or other and they would arrange as to who could come to the thing and they could operate under any system that they desired. It would depend upon a particular group. They could sell their tickets to anybody—I mean as far as they were concerned, but it was still the general public. The only difference would be was that it was their group who was sponsoring the party.

That in essence is what was done.

The agents assessed or set up the tax. The Commissioner assessed the tax and the plaintiff—the taxpayer here disputed the tax.

One of the things that appears in this case is a lack of records of the taxpayer to show any of these breakdowns, [23] for instance, as came up in a conference in chambers. That was brought up by Mr. Mortenson: "What were the receipts after the curtains in the Pavilion Room were drawn open at 10:30 and the show started? What were the taxable receipts?" We don't know. And the reason we don't know is that the taxpayer had no way or attempted in no way to segregate those receipts. In other

words, all the receipts of the Pavilion Room are entered either in food or drink records but they don't segregate as to what happened before the curtain was open or after.

And, secondly, and it isn't really an important part of the case, but it is one of the criteria we should look for and that is the fact that there was this door, just like this door in the courtroom, separating the back of the courtroom from the front through which people could go down to the main room and dance in the main room. In other words, they could go down and dance to the regular orchestra. There was a passageway leading from the Pavilion Room into the entry and then into the front room and they could go around that way and dance in the main room.

Now, I am not saying a large amount went there but it wasn't restricted. People could go back and forth, and dance and participate in the activities in that room.

Now, why is that important? Well, it is important because the statute says those people who are entitled to [24] go in and participate in the entertainment, anything paid by or for them is subject to the tax. That is what the statute says.

Well, it is the Government's position essentially that the Pavilion Room receipts are taxable; that they were just as much a part of this cabaret as the people in the main room who came there. Certainly the circumstances were different but mind you in a period of between June of 1951 and April 1st of

1955 there were some, almost 600 private parties in this period of two and a half or three years.

So, it was an integral part of Ciro's operations. There is no doubt about it as far as the closed-house parties are concerned.

The Court: How did you arrive at the figure of 304?

Mr. McHale: As to the Pavilion Room we don't know the exact number of parties. Ciro's has records of 304 parties. We don't know how many actually there were. There were probably a few more than that. Some files may have been lost. One group may have had a party two or three times during the period.

There are 255 of the Ciroette Room parties and approximately 50 closed-house parties.

The Court: But you said in your opening there were 304 Pavilion Room parties and just now you said 600.

Mr. McHale: I meant parties—what I meant was private [25] parties of all sorts. All I am trying to show is that this was an important part of the whole Ciro's cafe operations—the advertisements, the inducements held out to the public that they could see the show. That was all a part of the cabaret operation. That is all I am trying to point out.

There is no question that the evidence will show that the opportunity to go to Ciro's and see a show rather than to some place that would just be a restaurant or just some place where the people would hire their own orchestra and dance was an important thing that caused many of these groups to select

Ciro's. In other words, it was an opportunity to see the floor show and this was held out to the public by and large in advertising widely published in the metropolitan newspapers and in other ways during the period involved.

It is the Government's position that the burden of proof of showing any portion of these receipts are non-taxable is on the taxpayer.

The regulation specifically requires the taxpayer to maintain records showing this and there is no doubt that the evidence will show that the taxpayer did not maintain such records, although he could have done so.

Mr. McHale: There is one thing we didn't take up with the court. We do have the situation of a refund suit and counterclaim. I suppose the order of proof would be the same—that is, that the taxpayer would commence—— [26]

The Court: I should think so. We might as well take our short recess at this time.

(Short recess.)

The Court: There is one other thing to clear up, Mr. Mortenson.

In the event that I decide that the operation of the Pavilion Room is part and parcel of the main room operation, you are not contending that if that is so that there should be a breakdown in the apportionment of the tax for food served before the entertainment and charges after the entertainment.

Mr. Mortenson: Well, actually until I came into chambers this morning I didn't realize that this assessment had applied to anything but the pay-

ments for the private parties themselves. That was my understanding of the assessment.

Now, I assume this, without having given it too much thought, that if you deem the sales in the Pavilion Room to be taxable just like sales in the main room, then your judgment will be for the amount that is set up here.

I believe I am correct. Is that not right, Mr. McHale?

Mr. McHale: That is as I understand it.

The Court: I know what my judgment would be for, but I want to know what you contend. Would you agree there should be no splitting under those circumstances of the charges and the tax on the charges so that the tax—that the tax [27] will be a separate tax only for charges made after the entertainment went on.

Mr. Mortenson: Well, I don't really understand the question.

If sales in the Pavilion Room are taxable, we will say before 10:30, then they are bound to be taxable after 10:30.

The Court: I think you have answered my question.

Mr. McHales: Before we start, I meant to hand the court this earlier. I have made an analysis of the stipulation, joint Exhibit 2-B. If I may file it and serve a copy on Mr. Mortenson.

The Clerk: Mr. McHale, this is really going to be Plaintiff's Exhibit 2. You have indicated it is Exhibit 2 for you and B for the defendant. is that right?

Mr. McHale: That is how we had set it forth. It is just an analysis for the court.

The Court: This is not an exhibit?

Mr. Mortenson: If your Honor please, I have, of course, not seen this until just now. I notice on page 3 it begins:

"For almost all of the parties it was contemplated between Ciro's"

and so on.

This looks to me like an argument and I don't believe it [28] should be labeled "a stipulation."

The Court: It is not labeled "a stipulation."

Mr. McHale: It is our analysis.

The Court: It is not a stipulation. It is the Government's analysis of the stipulation and this is his interpretation of it.

Mr. Mortenson: I don't understand it being submitted now.

Mr. McHale: Well, you submitted a memorandum this morning.

The Court: All right.

Mr. McHale: I felt the exhibit itself was rather difficult to comprehend.

The Court: You are so right. I glanced at it the other day and the exhibit itself looked like a Chinese puzzle.

All right, Mr. Mortenson, do you want to proceed?

Mr. Mortenson: Before I call a witness should we introduce the exhibits which we have stipulated may be entered in evidence?

The Court: All right, let us do that.

Mr. Mortenson: We offer as Plaintiff's Exhibit No. 1.

The Court: What is it?

The Clerk: Additional tax assessed.

The Court: All right. [29]

(The exhibit referred to was marked Plaintiff's Exhibit 1 for identification.)

The Court: I usually like some sort of a brief description of what the exhibit is that you are offering. It may be received in evidence.

(The exhibit referred to was marked Plaintiff's Exhibit 1, was received in evidence.)

Mr. Mortenson: I offer as Plaintiff's Exhibit 2 a summary of the records pertaining to 304 private parties held in the Pavilion Room.

The Court: Received.

(The exhibit referred to was marked Plaintiff's Exhibit 2, was received in evidence.)

Mr. Mortenson: And there is offered as Plaintiff's Exhibit 3-A, 3-B, 3-C and 3-D. They are exemplars of agreements had with the chairman of the various private parties held in the Pavilion Room.

The Court: Received.

(The exhibits referred to, marked Plaintiff's Exhibits 3-A, 3-B, 3-C and 3-D, were received in evidence.)

Mr. Mortenson: And as Plaintiff's Exhibits 4-A, 4-B and 4-C, exemplars of typical advertisements placed by Ciro's in local newspapers.

The Court: Plaintiff's Exhibits 4-A, 4-B and 4-C admitted [30] in evidence.

(The exhibits referred to, marked Plaintiff's Exhibits 4-A, 4-B, 4-C and 4-D were received in evidence.)

Mr. McHale: I think the stipulation of facts should be offered also.

The Court: Yes; I have the original here.

Mr. Mortenson: I understand from the clerk that they had already been filed.

The Court: It is filed as a court paper. Do you want to offer it as an exhibit? I don't see that it is necessary to offer it as an exhibit unless you gentlemen want to do so. It is up to you.

Mr. McHale: That has been our custom.

The Court: How do you want to mark it?

Mr. McMale: These are really joint exhibits.

Mr. Mortenson: The others are plaintiff's so this should be, too.

Mr. McHale: There is one thing about this that I want to mention to the court with respect to paragraph 9 of the stipulation. It has to do with the use of the words "five per cent of the patrons of the Ciroette Room during the period involved did participate or witness the entertainment in the main dining room by being taken to the main floor by the management to witness the floor show at the conclusion of the Ciroette Room parties." I didn't mean this to convey the [31] idea that the Ciroette Room party was over at this stage of the game. I would like that part to be deleted.

The Court: Is that agreeable?

Mr. Mortenson: That is agreeable.

The Court: All right, we will strike out the words "at the conclusion."

Mr. McHale: Thank you, your Honor.

The Court: All right. It may be entered as an exhibit.

The Clerk: Plaintiff's Exhibit No. 5 in evidence. It is a stipulation of facts and is admitted in evidence.

(The exhibit referred to, marked Plaintiff's Exhibit 5, was received in evidence.)

PLAINTIFF'S EXHIBIT No. 5

In the District Court of the United States for the Southern District of California, Central Division

No. 20853-WM Civil

HERBERT D. HOVER, dba CIRO'S,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto through their respective counsel, without prejudice to the rights of any party herein to introduce additional evidence not consistent here-

Plaintiff's Exhibit No. 5—(Continued):

with and without prejudice to their right to object to the materiality or relevancy of any of the facts agreed to as follows:

I.

On November 14, 1955, the authorized delegate of the Secretary of the Treasury assessed against Herbert D. Hover, dba Ciro's, cabaret taxes for the period June 1, 1951, through March 31, 1955, in the sum of Sixty-seven Thousand Six Hundred Sixty Dollars and Sixty-two Cents ($67,660.62) taxes and Seven Thousand Eight Hundred Fifty-eight Dollars and Fifty-one Cents ($7,858.51) interest, for a total assessment of Seventy-five Thousand Five [32-A] Hundred Nineteen Dollars and Thirteen Cents ($75,519.13). Notice and demand for payment of the said taxes and interest was made upon the Plaintiff on November 16, 1955, and he paid the sum of Three Hundred Dollars ($300.00), and no more, on August 7, 1956. The outstanding balance of said assessment is Seventy-five Thousand Two Hundred Nineteen Dollars and Thirteen Cents ($75,219.13), together with interest as provided by law.

II.

The aforesaid deficiency assessment of cabaret taxes represented additional taxes assessed with respect to three phases of Plaintiff's operation for the period involved; the Ciroette Room; the Pavilion Room and the Closed House parties. There will be introduced into evidence as Joint Stipulation, Exhibit 1, the computation of Revenue Agent Bernard

Plaintiff's Exhibit No. 5—(Continued):

J. O'Connor, showing in detail by taxable periods the amount of additional assessed tax attributed to each of the aforementioned operations. Of the total assessment of Sixty-seven Thousand Six Hundred Sixty Dollars and Sixty-two Cents ($67,660.62), Nine Hundred Ninety-two Dollars ($992.00) is attributable to "main room operations" and is conceded to be due and owing by the Plaintiff because of a clerical error and is not in issue in this law suit.

III.

The amounts of the respective deficiencies in tax determined by the Revenue Agents who made the audit, was based on their examination of Plaintiff's books and records and applied the cabaret tax to a certain percentage of the receipts of each room on a basis that is more fully detailed hereinafter. The taxpayer did not consider the receipts of the said rooms taxable and, consequently did not, in his books and records, segregate any portion of the receipts as Federal cabaret taxes.

Facts Respecting the Pavilion Room

IV.

1. During the taxable period involved, Plaintiff operated the Pavilion Room on the same nights as the main room in which there was entertainment. Taxpayer has records showing the arrangements for 304 of the parties held in the Pavilion Room during

Plaintiff's Exhibit No. 5—(Continued):

said period. To be introduced into evidence as Joint Stipulation, Exhibit 2 is a summary of the Plaintiff's records regarding reservations of the Pavilion Room during said period, together with a key to the comments and information contained on such summary. Said Exhibit refers only to arrangements made in advance and does not purport to be evidence with respect to what actually happened at any of the parties involved. The tax shown in Exhibit 1 was not computed from the above records but from other books and records.

V.

To be introduced into evidence as Joint Stipulation, Exhibits 3-A through 3-D, inclusive, are authentic copies of representative records of the Plaintiff from which the summary, Joint Exhibit 2-B, was made.

VI.

To be introduced into evidence as Joint Stipulation Exhibits 4-A, 4-B, 4-C are advertisements of Ciro's, typical of the kind and type of advertisements run by Ciro's in its own and outside publications during the period involved.

VII.

With respect to the Ciroette Room, there is no issue as to the percentage of the receipts subject to the cabaret tax, Plaintiff conceding that if a tax is due as a matter of law, then 5% of the receipts are taxable.

Plaintiff's Exhibit No. 5—(Continued):

VIII.

Plaintiff maintained records showing receipts and the computation of the cabaret tax as reported on the tax returns, but Plaintiff kept no records showing what, if any, proportion of the [32-C] persons who attended the parties in the Pavilion Room stayed for the floor show or for dancing.

IX.

The Ciroette Room is a separate room on the second floor of the establishment reached by a stairway and the patrons of this room could not see or hear any part of the entertainment in the main dining room. Five per cent of the patrons of the Ciroette Room during the period involved did participate or witness the entertainment in the main dining room by being taken to the main floor by the management to witness the floor show ~~at the conclusion of the Ciroett parties~~. The only issue with respect to the Ciroette Room is whether, as a matter of law, the cabaret tax applies to this five per cent.

/s/ ERNEST R. MORTENSON,
Attorney for Plaintiff,

LAUGHLIN E. WATERS,

By /s/ EDWARD R. McHALE,
Attorney for Defendant.

Dated: 17th day of December, 1957.

Received in evidence December 19, 1957. [32-D]

Mr. Mortenson: Will you rise, Mr. Hover?

Your Honor, before I start my direct examination, is it your preference to have counsel stand when examining a witness?

The Court: Yes, it is. Do you have a different custom here in this District?

Mr. Mortenson: Well, the judges vary on that.

The Court: Yes, we always have them stand in New York. I have been sitting in San Francisco and some of them, off the record, must have gotten flat feet but they were standing. [32]

HERBERT D. HOVER

called as a witness on behalf of the plaintiff, being first sworn, was examined and testified as follows:

The Clerk: State your full name.

The Witness: Herbert D. Hover.

Direct Examination

By Mr. Mortenson:

Q. Mr. Hover, will you tell us something about your educational background?

A. Well, I attended Columbia University for over six years and I am a graduate of the Columbia University Law School and a member of the Bar of the State of New York, and a member of the Federal Courts for the Eastern and Southern Districts of New York.

I taught—I was an editor and publisher at one time and wrote articles.

The Court: Editor and publisher of what?

(Testimony of Herbert D. Hover.)

Q. (By Mr. Mortenson): You are the owner and operator of Ciro's, are you not?

A. Yes, sir.

Q. And how long have you operated Ciro's?

A. 15 years.

Q. Prior to that what was your occupation? [33]

A. Well, immediately prior to that I was associated with about four or five corporations. I was president of these corporations, one of which was a Hollywood restaurant corporation. I don't quite recall the others. One I think was called "Trans-National Talent, Hollywood Productions, Inc."

I did that for a period of four years, from 1938 to 1942, and before then I lived in New York where I practiced law and produced shows.

Q. Now, in addition to your writing for magazines are there any distinctions that you could mention here that would tell us something about your background?

A. Well, I am listed in Who's Who and am honorary chairman—I don't know whether this is a distinction or not, but I have been a star—I wrote, directed and produced one of the top shows for CBS.

I worked for NBC—ABC, which is the American Broadcasting Company. I had my own show which I wrote, directed, produced and starred in.

I wrote two scenarios for motion pictures which were bought and——

Q. Now, with regard to Ciro's. Are you personally familiar with the operations from June 1st, 1951, to April 1st, 1955? A. Yes, sir, I am.

(Testimony of Herbert D. Hover.)

Q. And your familiarity is due to your personal supervision, [34] is that correct?

A. Yes, sir. May I interrupt? You asked me something else. I was formerly a lawyer with the Federal Government.

Q. What department were you in?

A. With the Department of Commerce from 1933—during 1933 and 1934.

The Court: Let me interrupt for a moment, Mr. Mortenson. In those instances when music was piped in for dancing in the Pavilion Room, do I understand dancing actually takes place in the Pavillion Room?

The Witness: Yes, there is a dance floor there.

Q. (By Mr. Mortenson): Mr. Hover, there was an examination of your cabaret tax returns by two agents by the name of O'Connor and Ross, is that correct? A. Yes, sir.

Q. Subsequent to that examination did you receive a report concerning a proposed assessment?

A. Yes, sir.

Q. Mr. Hover, will you give a description of the physical layout of the first floor of Ciro's?

A. Well, the first floor—what was generally referred is the "main room," is rectangular in shape and there is, as you described, there is a band stand corresponding to where the judge is sitting, and directly in front, which is [35] elevated, directly in front is a dance floor and around the dance floor are tables, chairs and tables.

And looking eastward we walk up three flights

(Testimony of Herbert D. Hover.)

of stairs and we have what might be considered another room. We refer to it as "the lounge" and south of the lounge is a foyer through which you went into the main building.

And further east in back of the lounge is another building and in this building is the Pavilion Room, which is approximately three steps above the lounge.

In the lounge we have an extra step and then from that elevation there are two steps into the Pavillion Room.

As you enter Ciro's from the foyer into the lounge you face west for the dance floor and the orchestra, but as you went to the Pavillion Room from the street the dance floor and the orchestra, you would face south to view the dance floor and the orchestra.

Q. Now, will you state the history of the Pavillion Room—its construction?

A. Well, it was constructed in 1951 and was opened in 1952.

It was put up there basically for private parties. We had been doing some private parties. We had opened a room in 1948 which we called the "Ciroette Room" and it was a rather small room so we constructed another room which we called the "Pavilion Room" which was put in another building.

Q. As far as the Pavilion Room is concerned then, as I understand your testimony, it is in a separate building from the one in which the main room was located and the lounge—it is in a separate building but the two buildings were joined?

(Testimony of Herbert D. Hover.)

A. Yes, sir. Under the building code it is classified as a separate building. It was also constructed about 20 or 30 years after the construction of the Ciro's building.

Q. Mr. Hover, I show you a document. It bears the notation at the top "Name and address of taxpayer. Herbert D. Hover, D.B.A. Ciro's, 8433 Sunset Boulevard, Los Angeles, California," and that is dated 9-29-55. "Examining officers B. J. O'Connor, Chester M. Ross," and I will ask you whether this is a document which you kept in the regular course of business? A. Yes, sir, it is.

Mr. Mortenson: This is offered as Plaintiff's Exhibit next in order.

Mr. McHale: I object to the materiality and relevancy of this document. It does not bear on any of the issues in this case.

The Government has assessed the tax. The assessment is the key here and not a document.

The Court: What is the relevancy?

Mr. Mortenson: The relevancy of the document, your Honor, [37] is the basis for the assessment.

This document bears the breakdown of the taxes and the amount of the assessment. It is a further explanation of the joint or Plaintiff's Exhibit 1.

The Court: Where is Exhibit 1?

(Document handed to the court.)

The Court: Oh, yes. What do you mean by "a further explanation"? Isn't Exhibit 1 complete enough?

(Testimony of Herbert D. Hover.)

Mr. Mortenson: No, your Honor.

The Court: Let me look at this. Is there any conflict between the figures in Exhibit 5 for identification and 1 in evidence?

Mr. Mortenson: No, your Honor.

The Court: I will receive it in evidence.

Mr. McHale: There is one further thing, your Honor. May I be heard again on this?

The schedules are here. We have no objection to it but the preliminary statement which I believe is on page 3 we do object to as the reason—as I understand Mr. Mortenson's statement, the reasons the Government made for assessment is contained, or the reasons are contained therein. We don't believe this is material or relevant. If it is this is but a part of the report, the report upon which the Government acted which is contained in several other pages which are not sent to the taxpayer. [38]

For that reason we feel that this page 3 should be excluded and if not then the entire report should be introduced into evidence.

The Court: Where is the entire report?

Mr. Mortenson: We have no objection to that.

The Court: Do you want to introduce the balance of the report? Do you want to do that now or do you want to do it later?

Mr. McHale: I will do it later.

The Court: Then let it be marked for identification.

Mr. Mortenson: I will offer it now.

The Court: Very well.

(Testimony of Herbert D. Hover.)

The Clerk: Plaintiff's Exhibit 6 marked for identification and admitted.

Mr. Mortenson: In stipulating that the rest of that report may go in, I am thoroughly conscious of the fact that it is going to have a lot of self-serving statements in it and I know that the judge will consider that in reading the report.

The Court: Certainly. As a matter of fact, basically, that is the reason why I have admitted this. I think the judge is, as distinguished from a jury, capable of deciding what he should give weight to and what he should not give weight to.

Mr. Mortenson: Precisely, your Honor. [39]

(The exhibit referred to was marked Plaintiff's Exhibit 6 and received in evidence.)

The Court: Go ahead.

Q. (By Mr. Mortenson): Now, in this report that was made out by the agents, there are three categories of assessments, Mr. Hover. Is that correct? A. Yes, sir.

Q. And you understand the theory on which the Government has assessed these taxes, do you not?

A. I believe I do. You mean the theory being used at this time?

Q. Yes.

A. The theory has changed from time to time.

Q. Yes. Now, starting with the Pavilion Room parties. You know that 304 of them are involved here by stipulation, do you not? A. Yes, sir.

Q. Now, with respect to the parties held in Pa-

(Testimony of Herbert D. Hover.)

villion Room that are in issue in this action, will you explain how arrangements were made with the representatives of the groups that held those parties?

A. Well, the contract would be entered into relating to the dinner to be held in the Pavillion Room.

It was invariably a signed contract and it stipulated the time when the party would come in. There was stipulated [40] a uniform dinner for every person. The dinner would normally be a uniform dinner for everyone.

The price—and it would be subject to state tax, which I believe was four per cent although it may have been three per cent during part of this time. And also payment of the tip.

It stipulated the number of people who would attend. In other words, the contracts would normally stipulate between two figures, let us say, between——

Q. Just a moment. I show you Plaintiff's Exhibit 3-A and ask you whether that is one of the contracts you are speaking about.

A. This is a contract but it is not a typical contract.

Q. Take Exhibit 3-B. Would you say that is a typical contract?

A. No, sir. It is a contract but it is not a typical contract.

Q. Now, with respect to these parties—I mean the 304 which are listed in Plaintiff's Exhibit 2, you had 304 written contracts, is that right, one for

(Testimony of Herbert D. Hover.)

each party? A. Yes, sir.

Q. Then let us go back now to the typical contract. What would be the provisions, forgetting about this exhibit for the time being?

A. Well, the menu would be stipulated, the price per [41] person, the payment of the state tax and sometimes it would be plus gratuities and at other times a gratuity would be set forth such as 10 or 12½ per cent; the time the people would come in, the approximate number with the provision that a more definite number would be given to us like three days before the party, which would constitute the minimum guarantee.

Also included was the price of drinks and the time of arrival and the time the dinner would be served. The deposit and——

The Court: How about departure time?

The Witness: Departure time? I don't think so. It was not in the contracts, no, sir.

The Court: May I see one of the contracts?

(Document handed to the court.)

The Court: I am now examining Exhibit 3-A. This has gone into evidence, has it not?

The Clerk: Yes.

The Court: You haven't marked it in evidence.

The Clerk: I have it marked on my master sheet.

The Court: What was the reason for providing in here, Mr. Hover, that the drinks will be charged

(Testimony of Herbert D. Hover.)

for at the rate of 75 cents per drink until show time and 90 cents per drink thereafter?

The Witness: Well, many parties would want a bar open [42] for only one hour or an hour and a half. In that case we would not have to hire an extra bartender. We would use one of the bartenders regularly on duty.

It would be 75 cents if they used a regular bartender, but if they wanted an extra bartender it would cost us about $20 for the evening which would mean that we would have to take in about $30 more to pay for the bartender.

The Court: My question is why is there a specific reference "until show time, 10:30 and then 90 cents per drink thereafter"?

The Witness: I am trying to explain that, sir.

The Court: What I am trying to get at is, was there anything held out to the individual that they could see the floor show?

The Witness: In some cases, yes.

Q. (By Mr. Mortenson): Pardon me. I don't think you made clear, Mr. Hover, the relationship between the 90 cent drinks and the 75 cent drinks insofar as an extra bartender was concerned.

A. May I explain that?

Q. Yes, explain that again.

A. If they wanted a bartender all night it would cost us about $20 more, so we charged—you see, when people call for a party they say, "What do you charge for drinks, for standard drinks?" And we say, "75 cents." [43]

(Testimony of Herbert D. Hover.)

Sometimes they would say, "What do you charge for de luxe brands," and we say, "90 cents."

Now, if they wanted a bartender all night we would tell them from 10:30 on the drinks would have to be 90 cents.

The Court: That is what I am getting at. Why is it 10:30?

The Witness: Because until that time we could double up on our bartenders and by doing that the bartender wouldn't cost us anything extra. We would charge 75 cents a drink as long as we could use one of the regular bartenders.

The Court: What happens after 10:30? Why couldn't you double the bartenders after 10:30?

The Witness: That would mean we would have to have a bartender on all night for that bar.

The Court: I daresay that is not clear to me. Is it clear to you, Mr. Mortenson?

Mr. Mortenson: Yes. First of all I will explain the situation of the bar in the Pavilion Room.

Q. (By Mr. Mortenson): First of all, how many bars do you have in Ciro's?

A. We have four bars. We have a service bar which is in the kitchen. We have a bar in the lounge. We have a bar in the Pavilion Room and we have a bar in the Ciroette Room.

Now, let us say we had two, or let us say we had three [44] bartenders on duty. Now, if we had three bartenders on, and if there was a party in the Pavilion Room we could double one of those three bartenders in the Pavilion Room if they wanted him

(Testimony of Herbert D. Hover.)

only until the early part of the evening—until after 10:30.

If they wanted them beyond 10:30 that meant we had to get an extra bartender in which costs approximately $20.

The Court: I still want to know why it is at 10:30. Is there something sacred about 10:30?

The Witness: Because the show would go on shortly after 10:30 and that meant the bartenders would be busy at the other bars. The bartenders would not necessarily be busy before 10:30 so we can take one of those bartenders and move that bartender into the Pavilion Room, but after 10:30 if they wanted a bartender that meant we had to get an extra bartender and pay him for a full night's salary. Up until 10:30 supplying a bartender to the Pavilion Room did not cost us anything extra.

The Court: What time does the show go on?

The Witness: It goes on sometime between—if we did two shows, the show would normally go on between 10:30 and 10:45. At that time the bars would not be busy.

The Court: After 10:30?

The Witness: After 10:30. And that means we can bring the man back. [45]

The Court: Then if you can bring the man back my point is why should the price go up?

The Witness: After 10:30?

The Court: Yes.

The Witness: Because if we want a bartender all

(Testimony of Herbert D. Hover.)

night that meant we would have to hire an extra bartender for the Pavilion Room.

The Court: You mean after the show was over when you had to move the bartender back to his bar at 11:30 and they start serving drinks again?

The Witness: We would need—in other words, if anyone wanted a bartender to stay after 10:30 it meant we had to get an extra bartender because we would need the regular bartenders some place else—we would have to get an extra bartender at a cost of $20 to serve the party in the Pavillion Room.

The initial price we quoted for drinks was 75 cents. If they asked about de luxe or name brands we would say they are 90 cents and if they wanted a bartender all night it would be 90 cents after 10:30 because we didn't want to go back on our word as far as charging more than 75 cents a drink.

Q. (By Mr. Mortenson): Now, I understand then that the 15 cent differential between 75 cents and 90 cents was to pay for a bartender you had to bring in because they [46] wanted service until closing time, is that correct?

A. Because they wanted service, yes, sir, until—for an indefinite hour after 10:30.

Q. And whether the bartender came in at 10:30 or 11:00 or 11:30 you would still have to pay him for a full shift, is that correct—is that the way it works?

A. No. If we needed a bartender to stay after 10:30, we have to have an extra bartender and pay him. A bartender could tend bar in one of these

(Testimony of Herbert D. Hover.)

private rooms until 10:30. It would not cost us anything extra up until approximately 10:30. It would not cost us anything extra and therefore we charged the private parties 75 cents a drink as distinguished from a $1.10 a drink which we normally charge.

The Court: I am confused again. I thought you told me between 10:30 and 11:30 the bartenders are not busy and you can take a bartender from another bar and move him into this Pavilion Room where the private party is without hiring another bartender.

The Witness: I am sorry. I wasn't very clear.

The Court: Now, then, what is the story between 10:30 and 11:30 when the show is on you said—I thought I understood you to say the bars are not too busy.

The Witness: That is right.

The Court: And therefore you could take a bartender from one bar and move him to another where they needed extra [47] service.

The Witness: Well, sir, I think I can be a little more explicit if I use an example.

Let us say we have three bartenders on duty.

The Court: Three separate bars?

The Witness: Yes. We would have one, let us say, in the service bar, one in the lounge and one, let us say, in the Pavillion.

The Court: All right.

The Witness: Now, up until this time it did not

(Testimony of Herbert D. Hover.)

cost us anything extra to put a bartender in the Pavilion Room because at 10:30, or, let us say shortly after 10:30 the show would start and the bars were not very busy, so the bartender in the service bar, which is located in the kitchen—he would normally stay where he was during the show time. One of the other two bartenders, the bartender at the front bar or Pavilion bar—he would relieve the other bartender who had gone to eat. We would have three bartenders, two in the lounge and one in the service bar. Let us say that at 11:00 o'clock we got very busy—it would be at its maximum.

Now, if we had to have a bartender in the Pavilion Room all night we could not do that.

The Court: By "all night" you mean until 2:00 in the morning?

The Witness: Yes, sir, 2:00 in the morning. In that [48] case we have to have four bartenders instead of three.

The Court: But you speak in terms of "all night." I want to get that clear in my mind.

In this contract, which you say is not a typical contract, Exhibit 3-A in evidence, there is just a flat statement that 75 cents per drink until show time at 10:30 and 90 cents per drink thereafter.

The Witness: Show time at 10:30.

The Court: Yes; and 90 cents per drink thereafter. And they will be paid for by the individuals ordering them. Was that the customary thing with these private parties when they stayed on beyond the end of the show?

(Testimony of Herbert D. Hover.)

The Witness: No, sir; that was more of a stock clause because you see, mostly they didn't stay on.

You see, they would let us know in advance "We will be through at 10:00 o'clock." Most of the parties were through at 10:00 o'clock but we put these clauses in because you sign a contract like this, let us say, and then a day or two before the party they will say, "Well, I think we are going to go until 2:00 o'clock in the morning."

We protected ourselves by putting in the 90 cents for a drink.

The Court: My question is, supposing they go to 11:30, just after the show and leave. What happens then?

The Witness: Well, they don't, sir—most of the [49] parties were through by 10:00 o'clock but we have to protect ourselves by putting 90 cents per drink in there.

The Court: The point you are making is that most of the parties did not stay for the show?

The Witness: In many, many cases they did not, sir, but in any event the party was over by 10:00 o'clock.

The Court: What happened in the case where they did stay for the show? That is what I am trying to get. Did you leave at 11:30 right after the show?

The Witness: Yes, sir.

The Court: And then you say "Music from the orchestra in the main room will be furnished for dancing."

(Testimony of Herbert D. Hover.)

Does that mean dancing in the Pavilion Room or in the main room?

The Witness: Piped into the Pavilion Room.

The Court: That is all evening long before the show starts?

The Witness: Well, before we would have records playing until 9:30 or 10:00 o'clock and then our band would come on and usually they play what we call dinner music until about 10:30 and that is piped into the Pavilion Room. Then the show would go on shortly after 10:30 if we did two shows—about midnight if we did one show.

The Court: Go ahead, Mr. Mortenson. [50]

Q. (By Mr. Mortenson): Now, with respect to these private parties held in the Pavilion Room, will you explain in detail the difference in the operation in the Pavilion Room from that in the main room with respect to all features that you can recall?

A. Well, I anticipated that question, sir, and I jotted down some notes. May I refer to this, sir?

The Court: Surely.

The Witness: Well, a private dinner was confined exclusively to the group and the general public was not admitted. In the main room anybody could come in.

There was a difference in table set up—in the main room we had the normal cafe setup which usually consisted of round tables of varying sizes which would seat four or six or banquet tables seating two.

In these banquets we had the banquet setup which

(Testimony of Herbert D. Hover.)

was rectangular tables which seated eight, but normally I seated 16 to 20 people at a table. In the main room we seated approximately a half as many people in the same area. There was a cover charge. And for the private dinner parties there never was a cover charge.

In the main room the patrons sat wherever they designated but in the private dinner parties they seated themselves and they also controlled the seating arrangement and ordinarily we had a dais for speeches. [51]

Q. The people who came into the main room paid no parking fee?

A. The parking, incidentally, was operated by an independent concessionaire. The people who came into the private dinner parties paid a parking fee.

In the main room prices normally were $1.10 per one-ounce drink and for the private parties normally it was 75 cents—sometimes 70 cents a drink and sometimes lower than that.

In the main room the waiters served until closing time. We always stop the sale of beverages by 2:00 o'clock a.m. Sometimes people would stay until after 2:00 a.m.—they would stay until 2:30 or 3:00 o'clock in the morning. The waiter had to stay there. In the private rooms the waiters left as soon as dinner was served.

Q. Will you pardon me? You referred to only the Pavilion Room and the main room—you said "private room." You mean the Pavilion Room?

(Testimony of Herbert D. Hover.)

A. Yes; I meant the Pavilion Room where we served private parties.

The Court: Are you talking only of the Pavilion Room up to this point?

The Witness: Yes, sir. In the main room patrons came in without reservations and sometimes they would telephone in advance. In the Pavilion Room it was always a prearranged [52] affair—group reservations with a designated number.

In the main room a band can work only six days and we can use an out of town band. In the Pavilion Room, if they hired musicians, they had to be local musicians only—they could not use what are called "out of town musicians."

In the main room if a patron made a reservation and did not show up there was no liability.

The Court: With the hiring of a band—there is no contention here—I think the Government will concede if the Pavilion Room hires its own band there is no tax liability.

Mr. McHale: That is right.

The Witness: I am showing the difference between the two operations because the union recognizes the difference in the operation.

The Court: We are talking of those situations where they use the same entertainment.

The Witness: All right. In the main room if a patron had made a reservation and did not show up there was no liability. In the Pavilion Room there was liability up to the extent of the minimum guarantee.

(Testimony of Herbert D. Hover.)

In the main room there was no deposit made on a reservation. In the Pavilion Room there was always a deposit made.

In the main room the waiters worked on an eight-hour basis—in the Pavilion Room they worked on a four-hour basis. [53]

In the main room the waiters normally work from 8:00 to 2:00 or 3:00 a.m. and in the Pavilion Room they worked from 4:00 to 8:00 or 5:00 to 9:00 or 6:00 to 10:00.

In the main room the menus are a la carte. In the Pavilion Room the menu was prearranged and invariably they all ate the same food except sometimes on a Friday night there would be fish served.

In the main room each patron ordered and ate anything that he selected—in the Pavilion Room they all ate the same thing.

In the main room the prices were about 40 to 60 per cent higher than in the Pavilion Room. In the main room service was different, such as vegetables would be served in different dishes, while in the Pavilion Room the vegetables and the main order we usually served on the same plate and they were ordinarily much smaller portions.

In the main room we gave our waiters three meals a day. In the private room waiters who worked for us were served only one meal.

In the main room there was repeated trade at the same tables. That is, if some people had been sitting at a table and then left then other people

(Testimony of Herbert D. Hover.)

would come in and sit at the same table. In the Pavilion Room there was no repeat trade.

In the main room the tabs were individually paid. In the Pavilion Room all the dinners were on one tab. [54]

In the main room we presented our own shows. In the Pavilion Room there was no show at all, or if there was a show invariably they supplied their own show, unless later on some of the people did see our show in the main room.

In the main room there were no speeches. In the Pavilion Room normally speeches were made by people who attended with the group.

In the main room people normally came in at any time—usually after 9:30 and up until 1:30 a.m. In the Pavilion Room they generally came in about 6:00 or 7:00 o'clock p.m.

In the main room dinner was not compulsory—you can come in and have no dinner at all.

In the Pavilion Room unless it was an out and out cocktail party dinners were compulsory and had to be paid for whether eaten or not.

The Court: Would anybody have any objection if that were admitted as an exhibit? I would like to have it before me.

Mr. McHale: I haven't any—may I look at it?

The Witness: These are my own memos. There are some abbreviations on here.

Mr. Mortenson: May I see it?

Mr. McHale: I have no objection.

(Testimony of Herbert D. Hover.)

Mr. Mortenson: I will offer this as Plaintiff's Exhibit next in order. [55]

The Clerk: Plaintiff's Exhibit No. 7.

The Court: It is marked for identification and is admitted in evidence.

(The exhibit referred to, marked Plaintiff's Exhibit 7, was received in evidence.)

Mr. Mortenson: If there are abbreviations or misspelling, your Honor, I am sure the witness is taken quite by surprise. He shouldn't be embarrassed because it was intended only to refresh his memory and not to be introduced as an exhibit.

Q. (By Mr. Mortenson): Now, what was the method of handling tips or gratuities in the Pavilion Room?

A. Well, the tips were usually stipulated to in the contract, in the written contract, but in any event a lump tip was given to the waiters, to one of the waiters who divided it among all the waiters that served in the Pavilion Room.

Now, in the main room you tip whatever you wish and the waiter would keep it unless he shared it with his partner.

Q. (By Mr. Mortenson): Now, at what time would this single tab for the private party in the Pavilion Room be paid?

A. Well, usually about 10:00 o'clock. When the dinner was over. Might have been paid for at 8:00 o'clock or 9:00 o'clock. As soon as the dinner was over one of the men would pay the tab. [56]

(Testimony of Herbert D. Hover.)

The Court: You mean usually the chairman of the dinner party?

The Witness: Yes, sir.

The Court: And you usually would have had a deposit in advance, wouldn't you?

The Witness: Always had a deposit.

The Court: Running at about what per cent?

The Witness: Well, it wasn't based on a percentage. Usually it was $50. In some cases it was $100.

Q. (By Mr. Mortenson): Did the waiter in the Pavilion Room remove the dishes before they left the premises?

A. No, sir; the dishes stayed on the tables.

Q. Who did remove the dishes?

A. The bus boys would remove them at about 1:00 o'clock in the morning.

Usually when our second show was on they would go in there and remove the dishes, but all the dishes stayed on the table.

The Court: Did you use any of the same help at all in the main room?

The Witness: No, sir; we never use the same help—we never use the same help except in two instances. At one time the waiters, our waiters went to the waiters' union and got a concession which lasted a very short while, whereby they could work both rooms, but that only lasted a very, very [57] short while.

Another time, in the event of an emergency, for example, let us say we had more people coming into

(Testimony of Herbert D. Hover.)

the main room than we anticipated, we might want to use a waiter working in the Pavilion Room in the main room and then we paid him two nights' pay. But we can only do that in extreme emergencies.

A man wasn't permitted to work the Pavilion Room and the main room at the same time.

Q. (By Mr. Mortenson): In addition to paying him double salary there also was some arrangement with the union welfare fund, is that correct?

A. Yes. We even had to pay double union welfare fund. A man working in the Pavilion from 5:00 to 9:00 or 6:00 to 10:00, we had to pay four hours welfare fund. And even though we doubled him and paid him an additional salary, which was a greater salary, we had to pay him for eight hours in the main room and even though he only worked four hours we had to pay him for eight hours and also pay the welfare fund for eight additional hours. So we actually paid for 12 hours that one day for one man.

The Court: How long did that arrangement last where you used the same waiters?

The Witness: When we had the union concession?

The Court: Yes. [58]

The Witness: I am sorry, sir. I can't tell you that but I would guess a couple of months—just a few months. It was a very short while, sir. That is all I can say—maybe four months, perhaps two months.

(Testimony of Herbert D. Hover.)

Q. (By Mr. Mortenson): Now, I am sure the court would like to know about the doors.

The Witness: Pardon me. There is another difference in the Pavilion Room. A man could serve only 20 people in the Pavilion Room. Now, if by any chance, more people came to the party than we anticipated then we would have to pay a waiter 25 cents for each person over 20 that he served.

In the main room a waiter can serve an unlimited number of people. He can serve 50 people throughout the evening if it were possible to do that.

Q. (By Mr. Mortenson): Now, will you tell us the arrangement with respect to the men's room and the ladies' room as far as the Pavilion Room private parties were concerned?

A. Well, the men's room consisted of a wash room and then up about two or three steps where there was a base and then a door and that led into another room in which were the urinals and the latrines.

Now, if you went in from the Pavilion Room there was a separate door leading from the Pavilion Room into the men's room on the upper level and if you turned right you went [59] into the room where the latrines were and if you turned left you walked down two steps into the washroom.

Now, that same room was used also by the main room except the entrance to that was on a foyer through a different door—I am sorry, through the lounge—not the foyer, but through the lounge.

(Testimony of Herbert D. Hover.)

Q. Now, with respect to the ladies room. Where was that located and what doors were there to the ladies room?

A. Well, the ladies room is located right off of the foyer as you come in. Now, there is a short hallway between the Pavilion Room and the foyer and in that hallway is a door which leads into the ladies room. That is the present setup.

Before there were two doors, one leading into it at the upper level, into the ladies room from the Pavilion Room and one leading to the ladies room from the foyer.

Q. How many means of access are there aside from those to the Pavilion Room?

A. Well, access from the street—it has its own entrance. Then you can also go in from the foyer in the main building. Then if you open the wall you can go in there from the lounge. And then you can go in through a corridor which is located on the north side where the waiters normally come in from the kitchen.

And then it is also possible, but not done, to go in from the foyer into the lounge—into the men's room and then [60] from there go into the Pavilion Room.

The Court: Is this a convenient place to break for lunch?

Mr. Mortenson: Yes, your Honor.

The Court: How much longer do you think you will be with the witness on direct?

Mr. Mortenson: I would say an hour.

(Testimony of Herbert D. Hover.)

The Court: About an hour. About an hour. I want to make arrangements for us all to be able to go out and see the premises, as was urged upon me in chambers this morning.

When do you think we should do that?

Mr. Mortenson: Could we break in this afternoon in time to do it?

The Court: All right, if you want to try and make arrangements. What do you think, Mr. McHale?

Mr. McHale: I was thinking it probably would be advantageous for the court to see the premises early in the trial.

The Court: I think it is better, yes, so I will know what you are talking about.

Mr. Mortenson: Could we do it this afternoon?

The Court: After you finish your direct examination?

Mr. Mortenson: Yes.

The Court: And before we begin the cross-examination.

Mr. McHale: Yes. [61]

The Court: Maybe we will do that because I want to make arrangements for a car to take me out there.

Mr. McHale: The reporter will have to come along.

The Court: I hope you make arrangements for his transportation.

Mr. Mortenson: I will be delighted to have him.

The Court: Very well. We will reconvene at 2:00 o'clock.

(Whereupon, at 12:00 o'clock noon a recess was had until 2:00 o'clock p.m. of the same day.) [62]

Thursday, December 19, 1958—2:00 P.M.

The Court: You may proceed.

Mr. Mortenson: Your Honor please, before Mr. Hover goes back on the stand could I take a moment to see whether we understand each other about the questions you asked?

I have taken the position in my brief that the cabaret tax should not apply until the entertainment starts. There is a regulation providing that the tax starts a half hour before the entertainment starts.

Now, that isn't an issue in this case. I didn't think it was but I thought it belonged in the brief. I had misunderstood how the agents had applied the 20 per cent. I thought the 20 per cent tax that appears in the computations here was applied on the amount that was paid over by these private parties, but I now find that it was done in a different way. I am not sure whether this is right but I believe it was, that they applied the 20 per cent to what appeared on the books as non-taxable sales, which would include not only the amount paid on the tab but also any sales made in the Pavilion Room bar after the tab was paid.

Now, let me explain—this is what I understood the assessment was—of course all sales in the main

room carried a tax. The patrons were charged 20 per cent and that was paid to the Government. There is no issue about that. [63]

Now, forgetting about the closed house sales which were charged the way I thought the Pavilion Room charges were, the agents then took the sales which appeared on Ciro's books as being non-taxable and put the 20 per cent on that. They didn't do it by going to these folders for the 304 parties, but now I come to this. I understood you to ask whether——

The Court: Excuse me. Mr. McHale, the agent will explain, won't he, during the course of the trial how he arrived at the tax?

Mr. McHale: We can certainly do that. I thought it was clearly understood by Mr. Mortenson. I didn't realize there was any doubt about it.

Mr. Mortenson: If that is the way it was done we have no problem, particularly now since we have——

The Court: Would you explain how it was done then?

Mr. McHale: As I understand it they took the receipts from the Pavilion Room, if that is the one we are talking about, and applied the tax to the receipts of the Pavilion Room and it was from the books showing the receipts of the Pavilion Room and not from any folders or anything like that. They applied the same percentage with respect to the Pavilion Room as they did to the main room and it was 94 per cent and when they got to the Ciroette Room it was only 5 per cent.

Mr. Mortenson: There is no problem on that except this. [64]

Now, I think you asked whether it was my position if the sales from the beginning of the private party until show time were taxable—what is my position about the taxability after the show starts and I think I answered that if it is taxable before show time it has got to be taxable afterwards.

Mr. McHale: That is right.

Mr. Mortenson: But I wanted to be sure that I didn't have you understand that the converse was true, that if it were taxable from 10:30 on that doesn't mean it is taxable the other way.

The Court: All right.

Mr. Mortenson: All right, Mr. Hover.

HERBERT D. HOVER

called as a witness by the plaintiff, having been previously sworn, resumed the stand and testified further as follows:

Direct Examination
(Continued)

By Mr. Mortenson:

Q. Now, Mr. Hover, you have described to some extent how the accordion wall was situated between the Pavilion Room and the main room. Would you give us a little more detail about its structure?

A. Well, it was a permanent wall which is about three feet high and in the center of the permanent wall were two [65] doors and above that, up to—not the ceiling, but up to what we call the "fin,"

(Testimony of Herbert D. Hover.)

which is a decorative feature in the lounge, there was an accordion wall. On each of the accordion—on the accordion wall which faced the Pavilion Room we had a three-ply curtain which was drawn and that was part of the decorative effect of the Pavilion Room.

The Court: You say this was constructed in 1948 or 1949?

The Witness: No, sir; 1952.

The Court: Are there any architects' plans still available to show the layout and construction?

Mr. Mortenson: Mr. McHale and I looked at some here a couple of days ago but there were some changes made after that—after that plan was drawn up. I think I have it here, but it is quite an elaborate thing.

Mr. McHale: I think Mr. Hover could identify the changes.

The Court: If you think it will only complicate it instead of clarfying it that is up to you.

Mr. McHale: I think it would be a help. I don't think there is too much difference.

Mr. Mortenson: I have a thought in connection with this. Could we have it marked for identification and then perhaps have some other plans stipulated to base on it?

The Court: All right.

Mr. McHale: At this time it might be appropriate—this complete report that I spoke of this morning I have had photostated [66] so I could place it in evidence in lieu of the original and as

(Testimony of Herbert D. Hover.)

a part of it, as one of the pages, there is a sketch, admittedly not drawn to scale, but it is a sketch showing the layout.

The Court: All right.

Mr. Mortenson: If your Honor please, would you ask Government counsel to provide me with a copy?

The Court: He is doing that now.

Mr. McHale: I have a complete copy and it also includes the part that you put in evidence this morning, since it is all part of the same report.

The Clerk: Plaintiff's Exhibit 8 for identification.

(The exhibit referred to was marked Plaintiff's Exhibit 8 for identification.)

Mr. McHale: And this is Exhibit 6.

The Court: Do you want to mark it 6-A?

Mr. McHale: Yes, 6-A.

The Clerk: It is marked Plaintiff's Exhibit 6-A instead of Exhibit 8.

(The exhibit referred to was marked Plaintiff's Exhibit 6-A and received in evidence.)

The Court: Would it help you if I give this to you?

The Witness: Yes, your Honor.

The Court: Can you point to the Pavilion Room?

The Witness: Right here. [67]

The Court: This is your main room here to the left?

(Testimony of Herbert D. Hover.)

The Witness: Yes, sir; right up to here. There is the orchestra and the dance floor and the tables around here. This is the lounge.

The Court: Where do you enter?

The Witness: It is referred to as the foyer.

The Court: You enter here?

The Witness: Yes. This is the lounge and you go into the main room. In going to the Pavilion Room we enter here where there are some steps.

Mr. McHale: You are referring to the outdoor entrance?

The Witness: Yes, sir.

The Court: There is also an entrance through the main lobby, is that it?

The Witness: Yes, sir. Since this sketch was made we have opened a little hallway here where you can go from the foyer through the main hallway into the Pavilion Room and also from the men's room out here. And then there is—out here you go down this corridor which is what the waiters used.

Mr. McHale: This is a door?

The Witness: No; this is blocked off.

The Court: What is this room here?

The Witness: This is all part of the Pavilion Room.

The Court: What is this line of demarcation there?

Mr. McHale: This is an old wall that was removed. [68]

The Witness: Yes, sir.

(Testimony of Herbert D. Hover.)

Mr. McHale: And this would be where the accordion curtain is now?

The Witness: Right here.

Mr. McHale: And the double door would be in the center, is that correct?

The Witness: That is right, right here.

Q. (By Mr. Mortenson): That is a single door, is it not? A. I think it is double.

The Court: Let me ask you this: Where is the dance floor in the Pavilion Room?

The Witness: Right here. And there is your orchestra stand right here. There was a window here. The orchestra would be here and the dance floor is oval in shape like this and normally I face this way.

The Court: And the men's room over here. Is that a common men's room for both rooms?

The Witness: Yes, sir; from here and also from here.

The Court: Where is the ladies room?

The Witness: That is right here.

The Court: And that is a common ladies room, too?

The Witness: Yes, sir.

The Court: And where is the kitchen?

The Witness: The kitchen is here. [69]

The Court: Which serves all the rooms, is that right?

The Witness: Yes; the kitchen serves all the rooms in the entire building, both buildings.

The Court: All right, thank you.

(Testimony of Herbert D. Hover.)

Q. (By Mr. Mortenson): Mr. Hover, at show time did you on occasions move the accordion wall back? A. Yes, sir.

Q. Now, with the elevation of the Pavilion Room about how far back could the patrons in the Pavilion Room view a floor show down in the main room?

A. Well, I would say about 12 to 15 feet. In other words, about two tables back—two tables back might be 15 feet or 12 feet.

Q. With regard to the 304 private parties which have been listed in the Plaintiff's Exhibit 2, and you estimate the proportion of the patrons who stayed for the floor show after the moving of the accordion wall had been pulled back?

A. I would say in about 50 per cent of the cases —I would say in about—after the wall was pushed back only about 20 per cent of the cases and about 50 per cent of the cases nobody stayed to see the show, and approximately 50 per cent of these dinner parties—where anyone did stay, it varied anywhere from perhaps 2 or 3 per cent up to about 95 per cent and I guess a rough average would be approximately 50 per cent. [70]

The Court: You would say in about 50 per cent of the cases 50 per cent of the people stayed?

The Witness: At an average, sir. It might be very close.

The Court: You are not including the 20 per cent where the walls were pushed back?

The Witness: No. I say in about 20 per cent—about one case out of five we pushed the walls back.

(Testimony of Herbert D. Hover.)

The Court: So everybody would stay?

The Witness: No, sir.

The Court: How many would stay?

The Witness: Well, it might vary anywhere—in those instances it might vary from 33 to 95 per cent. There were always some people who left and many people could not see the show at all. That was about 20 per cent of the case, but in about 50 per cent of the cases people did stay for the show by coming into the lounge or part of the main room, where there was no cover charge. They could do that the same as people from the street could come in.

The Court: In 20 per cent of the cases the walls were pushed back and from one-third to 90 per cent or 95 per cent they would sit there and watch the show?

The Witness: Yes.

The Court: That leaves 80 per cent of the cases that you have to account for? [71]

The Witness: Yes, sir.

The Court: And of the 80 per cent 40 per cent would leave?

The Witness: No, sir. I would say of the 80 per cent five-eighths of the total nobody would stay and of the three-eighths—that is 30 per cent of the cases, some of the people would stay and some would leave.

Q. (By Mr. Mortenson): Now, when this percentage of people who stayed moved into the main room what was your practice with regard to charging cabaret tax and paying it over to the Government?

(Testimony of Herbert D. Hover.)

A. We charged cabaret tax and we paid it to the Government in all those instances.

The Court: Will you read the answer?

(Answer read.)

The Court: You didn't charge or pay a cabaret tax on the 20 per cent of the cases where you moved the wall back, did you?

Mr. Mortenson: No, no, your Honor. I think this question was intended to refer to the situation where the wall was not moved back but where the patrons from the private party walked into the main room.

The Court: There is no issue on that because there they would buy their drinks or whatever they were getting right in the main room. [72]

Mr. Mortenson: I wanted that to be clear. We have no problem in connection with that.

The Court: Yes.

Mr. Mortenson: But the members of the private parties who did stay and went into the main room or into the lounge, they were charged 20 per cent tax and that tax was paid over to the Government. The Government does not assert otherwise.

Q. (By Mr. Mortenson): Now, were there some groups that you can recall which never stayed for the floor show? A. Yes, there are.

Q. Did those groups come once or more than once?

A. Well, they were normally groups that would meet periodically like professional fraternities, like

(Testimony of Herbert D. Hover.)

a medical fraternity. Well, they might have 100 there and maybe of that 100, maybe none in some instances and in other instances two or three of the physicians would meet their wives after dinner in which case they would pay the federal tax on whatever was consumed in the main room.

Q. These individual members would then go into the main room and be treated like anybody else?

A. Yes, except that most times none of them walked in but occasionally some doctor would meet his wife in the lounge and he would stay there for a while.

Then there was a group of accountants and they would meet periodically. And one of the apparel guilds has been [73] meeting there for eight years and they would usually have speeches. At most all of these cases they would have speeches, professional meetings, business meetings.

Q. Now, with regard to the Ciroette Room, just briefly describe how you would go from the Ciroette Room on the second floor into the main room.

A. You mean from the main room to the Ciroette Room?

Q. Yes.

A. There was a door that you had to open and then walk down a flight of, I think 17 steps, and at the base of it you turned right. There was a fire door there and you walked through there and you were in the main room.

Q. Is there an alleyway that must be crossed

(Testimony of Herbert D. Hover.)

from a door downstairs to a door into the main room?

A. Well, as you reach the bottom of the stairs, if you turn left, there is sort of a fire door and alley which takes you outside. If you turn right you go into the main room.

Q. Now, in general without being specific, were the banquet facilities and the method of handling banquets in the Ciroette Room the same as in the Pavilion Room?

A. I would say substantially the same, yes.

Q. Were there differences in prices between the banquets in the Ciroette Room and those in the Pavilion Room?

A. Well, there was a slight difference. The prices of [74] food in the Ciroette Room were slightly less than in the Pavilion Room.

Q. And what about toilet facilities and checking facilities in the Ciroette Room? Were they separate or the same as those downstairs?

A. Well, we had a checkroom there—we had a men's and ladies' checkroom. We had something that corresponded to a checkroom and then a ladies' restroom and men's room there.

Q. Now, with regard to what we have designated here as the "closed house parties," did you have agreements with the representatives of the parties similar to the ones which have been entered in evidence here?

A. I don't think I have seen any agreements referring to closed house parties.

(Testimony of Herbert D. Hover.)

Q. Well, I was asking you whether you did have any. A. Yes, sir.

Q. You had them? A. Yes, sir.

Q. Now, in general what kind of arrangements were made as to these 20 closed house parties that have been assesed for cabaret tax in this case?

A. Well, there would be a stipulation as to the number of people, the menu, the price; a stipulation as to the tip, what time they would come in and sometimes there was reference [75] to entertainment. In some of these instances——

Q. How was the matter of the orchestra, if any, handled and how was the entertainment handled in most of these cases?

A. In most of the cases they provided—if they had entertainment they provided their own entertainment and music.

Sometimes they would take the show which was playing at Ciro's, or part of the show, and they would supplement it with their own acts. And in that case they would pay the people that had been working for us separately—that is, the money would not come through us. It would be paid directly to them.

In other words, if we had, for example, a name band or orchestra and if some of the people knew that band and wanted to make their own deal with that band and paid him separately—he worked for them and not for us on that particular night, but they specify the hours that he is to work—he works on a different scale of salary—a banquet scale—

(Testimony of Herbert D. Hover.)

they have a different number of men. In other words, he might have six men for them and play with us with 10 men or vice versa and whereas he worked for us four hours he might work five hours for them or any different arrangement.

He might start off with three men and supplement the band until he had eight men later on in the evening. Every deal was on its own, but they had full control of whatever [76] they wanted to do—whatever show they wanted. If they wanted a show or if they didn't want a show or wanted music or didn't want music, it was entirely up to them. Whatever they wanted they did it.

Q. Now, I used an illustration in my opening statement which I don't know was factually correct or not.

Suppose you had engaged Pearl Bailey for two weeks and somebody wanted a closed house party while Pearl Bailey had a two weeks' engagement with you—suppose it was right in between, what would happen there?

A. Well, if the closed house party was booked before we hired Pearl Bailey we would except that night from her contract and—let us say normally the contract would have been for two weeks, from September 1st to September 14th. The contract would stipulate that she would work her opening night, September 1st, but if the private party was on September 7 that she would not work on September 7 and would close on the 15th instead of the 14th

(Testimony of Herbert D. Hover.)

so that she would actually work 14 days out of the 15 days.

If the closed house was booked before we had signed Pearl Bailey, if the closed house was signed—was booked after we had signed Pearl Bailey the contracts had a clause that the management reserves the right to lay her off one day during that two week period and add that day onto the [77] end of the two weeks so you will get 14 out of 15 days and then we had a right to lay her off that one day.

In some instances an act wouldn't agree to that so in that case we had to pay the act even though they didn't work that night. But we had stock clauses in all of our contracts giving us the right on a two-week engagement to lay the act off one day and add the day on at the end of the engagement.

The Court: The question was what would happen if the engagement came during her two week period and she was the performer for the private party.

The Witness: In that case, if they wanted Pearl Bailey, they would pay Pearl Bailey.

The Court: What would happen is you wouldn't pay her?

The Witness: Not for that night.

The Court: Don't you have a contract with her for 14 days?

The Witness: Yes, sir.

The Court: What would happen on that one night?

The Witness: They would pay her for that one night.

(Testimony of Herbert D. Hover.)

The Court: In other words, they would pay her what you should have paid her—in other words, pro rata?

The Witness: Sometimes pro rata and sometimes less, depending on the day of the week. In other words, one night is more valuable than another. [78]

Q. (By Mr. Mortenson): Now, how were the arrangements carried out with regard to the closed house feature of the—strike that.

The Court: Let me ask you this. What would be the essential difference then on a closed house situation between a night when you opened it to the public and a night when the party had taken over the main room if you furnished the same entertainment and the same band?

The Witness: What would be the difference?

The Court: Yes, what would be the difference?

The Witness: Well, in one case the room is open to the public and in the other case it is not. In the other case it was a stipulated menu, it was a signed contract. Everything was on the tab. They could have whatever they wanted in the one case—no cover charge, but in the other case many of the tables have to pay a cover charge.

The Court: Perhaps I misled you with my question. What I wanted to get at, as far as the furnishing of the entertainment is concerned, would there be a difference?

The Witness: Yes.

The Court: What is the difference?

The Witness: Well, to begin with we took the

(Testimony of Herbert D. Hover.)

attitude that the people taking a closed house can do anything they wish.

Now, if they wanted to hire the act that was playing for [79] us at that time they had a right to do so because sometimes it was the only name act in town. They can have that act but instead of the act going on at a quarter of 11:00 and 1:00 o'clock as the act would normally do. Also they would have other acts in the show and the act probably would do a completely different show inasmuch as he or she did only one show that night. They might do a completely different show and the organization would pay for that act directly. In other words, when that act had a night off we didn't care whether the act worked or not.

The Court: You confuse me when you use the word "night off," I am talking about booking on a night when that act was supposed to work and the renting of the main room. Did you consider that a night off for the act?

The Witness: In most cases, yes.

The Court: You would consider that a night off for the act?

The Witness: In most cases I would.

The Court: I am assuming there is a two-week contract for the act and they are supposed to work every single night for two weeks and you have the medical association, let us say, renting the main room with your show for that night and your act and they don't import other acts—they want it as is. Now, in a situation like that, and I assume you

(Testimony of Herbert D. Hover.)

have had situations like that, is that correct? [80]

The Witness: Very few, sir. Maybe one or two occasions.

The Court: What course do most of them take?

The Witness: They bring their own show in.

The Court: Is that the usual thing?

The Witness: Sometimes they don't have a show at all. Other times they bring in their own and at other times will hire that act and supplement it with other acts of their own or with speeches or other embellishments. And sometimes a member of the organization would have a friend—maybe one would be Danny Thomas or Frank Sinatra or somebody like that who would have them go in the show and ad lib with the regular act.

Every party is on its own and we had no control over the show or the party. But we are assuming something, sir, which is a little bit contrary to what I tried to say and that is that in practice in every instance we had the right to lay the act off for that particular night because we had stipulated in advance of signing the act or, because the contract carried a clause we had a right to lay the act off for that particular night.

Q. (By Mr. Mortenson): As I understand you, when you say it was "night off" for the closed house party, that was one of the 15 nights provided for in the standard contract, is that correct?

A. Yes. [81]

The Court: He said when they signed them for

(Testimony of Herbert D. Hover.)

two weeks he had a right to ask them to take one night off and take the other night at the end of the two-week period, so there would be actually 15 days.

The Witness: Another way it would happen: sometimes we had an act for two weeks and they had not agreed to the clause. And during the time they opened we may have booked a private party and then when the act opens we will go to the actor and say we have a private party here on Sunday, "Would you be good enough to take that night off and we will add a day? You can take Sunday off," and in some cases they would agree. In one case the Hearst organization went to an act and asked them to do that and they said "Yes" and they said, "If you don't pay me for that night I will never work for you again as long as I live."

The Court: Is Ciro's operating now?

The Witness: Yes, sir.

Q. (By Mr. Mortenson): Actually, what we are talking about now is the 20 occasions from April 6, 1952, through March 27, 1955, or a matter of 20 parties in a period of three years, is that correct?

A. Yes, sir.

Q. And most of those parties were held on what day of the week?

A. Well, I can't tell from here but I would guess that [82] many of them were held on a Sunday night.

Q. Prior to the audit by Mr. O'Connor and Mr. Ross resulting in this assessment, had you been audited by treasury agents?

(Testimony of Herbert D. Hover.)

A. Yes, sir, we had been.

Q. Were the treasury agents familiar with the type of operation you had, for example, the closed house and the Pavilion Room operation?

A. They were thoroughly familiar—they knew everything we did and they agreed to what we did and——

Mr. McHale: I object to this question as immaterial and irrelevant and I move the answer be stricken.

The Court: I don't think it is material. It will be stricken.

Q. (By Mr. Mortenson): With regard to the closed house parties generally, who was at the door to take care of the patrons who were coming in and to exclude the public?

A. Well, we excluded the public. The parking attendants were told not to accept any cars from the public unless they stated they were coming in to this private party. And if anyone did get through, and there was also a big sign outside, I would say six feet by four feet saying "Sold out, please go to the Mocambo," which is a competitor close by.

Now, if they disregarded that sign and got through [83] the parking lot attendant, which happened very seldom, I was always at the door myself —the head waiter and myself were at the door, but I was always at the door myself and we did not let anybody in. We stopped them at the foyer—the door leading into the foyer, or if they got into the foyer

(Testimony of Herbert D. Hover.)

we stopped them at that time and told them they were not permitted to come in.

Q. Now, will you tell us whether anybody from the public was permitted to join any of these closed —so-called closed house parties?

A. Was anyone of the public permitted, is that your question?

Q. Yes. A. The answer is no.

Q. That is all I have, your Honor. I finished sooner than I thought.

The Court: All right. Well, I have asked for a car at 3:00 o'clock. I suppose you are all ready to go now, aren't you? Or do you want to start your cross-examination?

Mr. McHale: I thought it would be better probably to go out there now.

The Court: How long do you expect to be on cross-examination?

Mr. McHale: I think probably an hour or two—I am not sure. [84]

The Court: All right. We will recess from the courtroom to the premises that are in issue, Ciro's restaurant, and we will reconvene there.

I take it you can leave now and as soon as my car comes I will leave and meet you at Ciro's restaurant.

As I understand, you have arranged transportation for yourselves and the reporter.

Mr. Mortenson: Yes, your Honor.

(Whereupon, at 2:35 o'clock p.m. the parties indicated proceeded to Ciro's restaurant in Los

(Testimony of Herbert D. Hover.)

Angeles, whereupon the following proceedings were had:)

The Court: Let the record show that counsel and the court and the witness Hover have adjourned to Ciro's restaurant, together with the official reports, and that we are now inspecting the premises.

Now, what is this?

Mr. Mortenson: The Pavilion Room.

The Court: In the lounge the patrons always pay the 20 per cent tax?

The Witness: When the music is on.

The Court: From that point on, is that correct?

The Witness: No, about 30 minutes before.

The Court: Gentlemen, would you like to describe in your own words what you have seen here?

Mr. McHale: One thing should be clarified and that is [85] that since the period involved in this suit there have been some changes. I think Mr. Hover can probably tell us precisely what they are. But I believe this latice work screen—that is of rather recent vintage—or shutters.

The Court: You mean between the lounge and the main room?

Mr. McHale: Yes.

The Court: How long has that been there, Mr. Hover?

The Witness: That was put up in May of 1956. Before then we had curtains. You see there is a track there where we had curtains.

Mr. Mortenson: I think we can see the curtain tracks are still there.

(Testimony of Herbert D. Hover.)

Now, what kind of curtains were they?

The Witness: Well, they were heavy curtains.

The Court: Which could be drawn back.

The Witness: When the show was on they were opened and normally when we opened the room, the curtains were closed.

Mr. McHale: When the show was on the curtains were open all the way across?

The Witness: Yes, sir.

Mr. McHale: With complete visibility?

The Witness: Except the curtains took a certain amount of space.

Mr. McHale: Even the patrons at the bar could see the [86] show.

The Witness: You say the bar or lounge?

Mr. McHale: I mean the bar lounge.

The Witness: Yes, I would say they could except when the show was on sometimes the show is on the right side of the room. You see there is a stage over there on the right side of the room. You see those little bannisters there. That is removable and that is a stage that is elevated. That is a special event—sometimes we did the show up there.

Mr. McHale: And in addition in the lounge there have been a lot of new tables or chairs put in here, haven't there—in the lounge area, that weren't in existence during the period?

The Witness: Some of these we put in. That is a new table there—four new tables and by "new" I mean dating back to 1956.

(Testimony of Herbert D. Hover.)

Q. (By Mr. McHale): You didn't have all these booths in here at the time, did you?

A. No, sir.

The Court: How many more booths did you put in here?

The Witness: Well, there are four booths here sir.

Mr. McHale: And the ones in the middle—did you have them in the middle at that time?

The Witness: Well, they are new. I am trying to recall [87] what we had there. I know we had chairs and tables there at one time. We had a sort of what we call a banquet space in that room and we moved that and put these booths in, but I think it was a period of time when we didn't have anything there—just chairs and tables.

The Court: This mens room over here. Was that available only for those in the Pavilion Room?

The Witness: Yes, sir.

Mr. McHale: No—that connects with both rooms, does it not?

The Witness: This is available only—I think the judge pointed over here. No one else was permitted in this room.

The Court: Is that a common mens room?

The Witness: Common mens room.

The Court: Two entrances?

The Witness: Yes.

Mr. Mortenson: That is the one he described as having an entrance at two different levels.

The Court: And there is a ladies room we

(Testimony of Herbert D. Hover.)

haven't seen, I take it. We will get to it in a moment, which is also used commonly between the Pavilion Room and the main room?

The Witness: Yes, sir.

The Court: All right, gentlemen. Do you want to describe [88] your observations and I can join in.

Mr. Mortenson: We note there are three steps from the main room up to the lounge, one step in approximately the middle of the lounge and two steps from the lounge up to the Pavilion Room. That is from the upper portion of the lounge. That makes a difference of six steps from the main room to the Pavilion Room.

The lower wall separating the lounge from the Pavilion Room is approximately three and a half feet high, eight inches thick with a double door approximately in the center of the wall.

The Court: Also about three and a half feet high.

Mr. Mortenson: The accordion walls——

The Court: What would you say is the height between the floor and the ceiling here?

Mr. Mortenson: Approximately five feet.

The Court: From the floor?

Mr. Mortenson: From the floor to the ceiling?

The Court: Yes.

Mr. Mortenson: Approximately eight feet.

The Court: So that the accordion walls make up the difference between the permanent three and a half foot wall and the ceiling?

Mr. Mortenson: That is correct. And the accordion walls move back to the north and south walls

(Testimony of Herbert D. Hover.)

within approximately [89] five feet of the north and south walls.

The accordion walls are manually operated.

On the Pavilion Room side are heavy curtains made of three-ply fabric which close completely on a traverse rod.

Mr. Hover, would you show us how the cloth curtain pulls across?

The Court: I don't think it is necessary to show how it pulls across.

Mr. Mortenson: I guess we will all agree that the cloth curtain and the accordion wall draw back—you are at liberty to call it what you want, Mr. McHale.

Now, at the east end of the room is a bar at which presently there are four stools. The bar will hold approximately eight stools.

In the lounge at the north end is a bar which is large enough to accommodate about ten stools, ten patrons sitting down.

There is a separate entrance to the Pavilion Room leading from the street, the doors facing south. There is a door to the mens room on the north side of the Pavilion Room.

Before we get to the rest shall we look at the ladies room arrangement?

Mr. McHale: I would like to state for the record that the opening—— [90]

The Court: Wait a minute. I am going to give you an opportunity to describe it as you see it and then I may want to make some observations of my own.

(Testimony of Herbert D. Hover.)

Within our immediate vision this is all you see now that you care to describe for the record?

Mr. Mortenson: Except for an oval dance floor which has an approximate diameter of 13 feet by 16 feet in the center of the Pavilion Room.

South of the dance floor there is a grand piano up against the wall in an alcove. That is all I have here.

The Court: Do you want to say anything, Mr. McHale?

Mr. McHale: Yes, your Honor. I would say this. I think the solid walls separating the Pavilion Room from the lounge is closer to two and a half to three feet in height; that the sliding curtain when pushed all the way back opens to within approximately three feet of the side of the Pavilion Room on either side, leaving the entire center of the Pavilion Room open.

The Court: Will you approximate what that portion is that is open? The reporter suggested 24 feet. Would you agree, gentlemen, that when the accordion wall and the door and the curtains are open there are about 24 feet of clear vision?

Mr. Mortenson: I stepped off 24 feet.

The Court: Would you agree it is 24 feet? [91]

Mr. Mortenson: Yes.

Mr. McHale: I got 25 feet.

The Court: All right.

Mr. McHale: I would say that the difference in height between the seating level of the Pavilion Room and the dance floor of the main lounge is

(Testimony of Herbert D. Hover.)

such that the person sitting in the Pavilion Room would have clear visibility over the heads of the people seated intermediately in the lounge and main dining room.

Mr. Mortenson: And let the record show that Mr. McHale is sitting approximately where the sliding wall is.

Mr. McHale: The stage of the main dining room and the dance floor, I would say, is visible from most parts of the Pavilion Room except the back corners near the bar and the very extreme left and right side near the curtain.

I would say this for the record. It is my understanding that the furnishings and booths and so forth in here now are not those that were here at the time involved. I believe that is true, isn't it, Mr. Hover?

The Witness: Yes, it is, but the room itself is the same.

Mr. Mortenson: May I ask whether the legs on the chairs are the same length as they were?

The Witness: Yes, sir.

Mr. McHale: That is all, your Honor. [92]

The Court: I want to ask Mr. Hover a question. Is this Pavilion Room used on occasions for an overflow of the patrons of the other rooms?

The Witness: Yes, sir.

The Court: You just draw back the curtains and the accordion walls?

The Witness: No, sir; we always—we have another curtain here which, incidentally, is placed

(Testimony of Herbert D. Hover.)

where there are supports on each wall and where we had a very large attraction then we would draw this curtain and we could incorporate this portion of the Pavilion Room into the main room, but we would never go further than about here.

The Court: Mr. Hover has indicated that the front portion or the western portion of the Pavilion Room itself, approximately 20 feet of it, has been used on occasions to form a contiguous room with the lounge and the main room to handle overflow patronage with the curtains drawn back.

My observation also is that the lounge is contiguous with the Pavilion Room, lowered two steps and that the lounge is contiguous with the main floor lowered three steps.

Mr. Mortenson: And your Honor, if you will note, strangely enough, about the center of the lounge is another step.

Mr. McHale: I don't know whether I mentioned the width of the opening. It is approximately five feet between the [93] lounge and Pavilion Room.

The Court: All right, gentlemen. Now let us see the ladies' room from the outside. It has already been indicated there is a separate entrance from the outside to the Pavilion Room.

I also observe that there is a separate entrance into the Pavilion Room through the main foyer which serves as an entrance also to the lounge and to the Pavilion Room.

There is also a common ladies' room as there is a men's room for use for the two rooms.

(Testimony of Herbert D. Hover.)

All right, let us see the Ciroette Room.

The Witness: There is a separate checkroom here.

Mr. Mortenson: May we also note that there is a separate checkroom. There is a checkroom opposite the door leading into the Pavilion Room.

The Court: And also a checkroom, I take it, which the Pavilion Room people can use in the main foyer.

The Witness: Yes, sir.

Mr. McHale: There are also some loudspeakers in here, Mr. Hover. Now, whether they are in the same place as they were then I don't know.

The Court: I couldn't say.

Mr. McHale: There were speakers in the room?

The Witness: Yes, sir.

Mr. Mortenson: Now, I wonder if Mr. Hover could explain [94] the structure of this building in terms of the different levels?

The Court: That you can do from the witness stand tomorrow. You don't have to do that here because that is apparent.

Mr. Mortenson: We could look at if it has something to do with the basement.

The Court: All right, let us see the Ciroette Room.

Mr. Mortenson: We are now in the Ciroette Room. There is a window facing—there is a window on the north end—am I correct? That is north, is it not?

The Witness: Yes, sir.

(Testimony of Herbert D. Hover.)

Mr. Mortenson: And two exits on the west, one on one level of the Ciroette Room and a second level to the south.

The Court: I think that portion of it is really not important. I think what you should dictate for the record is your observation that there is ingress and egress down to the main room.

Mr. Mortenson: Yes, your Honor, that is true.

Mr. McHale: There isn't too much in the Ciroette Room.

The Court: No, there isn't.

Mr. McHale: I mean they are only taking five per cent from this room.

The Court: Are you going to present the five per cent part? [95]

Mr. McHale: Yes.

The Court: At any rate let me say this. My observation is that the Ciroette Room is located one flight up of approximately 13 steps.

The Witness: 17.

The Court: 17 steps to reach the Ciroette Room and you enter into a sort of bar and dance floor and then you climb another five or six steps in order to get into the dining portion of the Ciroette Room.

The Ciroette Room does not have any vision into the main room or the lounge and is, as I have said, one flight above it.

In order to enter into the main room you descend this flight of steps and go through a double door into the main room.

How do you get into this room? Do you go through the main foyer?

(Testimony of Herbert D. Hover.)

The Witness: You can go through the foyer or sometimes through another corridor which takes you outside.

The Court: But ordinarily it is through the foyer and through the lounge?

The Witness: Yes, sir.

The Court: And then upstairs?

The Witness: There are 14 steps.

The Court: 14? [96]

The Witness: Yes, sir.

The Court: Through the foyer and lounge and up here and they use the common check room downstairs.

The Witness: Well, we have something here which can serve as a checkroom. We have some hooks here but sometimes they will use the common checkroom.

The Court: Does anybody else have anything for the record?

Mr. McHale: You might mention there is a dance floor here.

The Court: I mentioned that.

Mr. Mortenson: There are separate toilets, separate toilet facilities for men and women here.

The Court: Unless somebody else has something to say we will recess court until 10:00 o'clock tomorrow morning.

(Whereupon at 4:00 o'clock p.m. a recess was taken until 10:00 o'clock a.m., Friday, December 20, 1957.) [97]

Friday, December 20, 1957—10:00 A.M.

The Court: You may proceed.

The Clerk: 20853, Herbert D. Hover vs. United States of America for further court trial.

Mr. Mortenson: Ready for the plaintiff, your Honor.

Mr. McHale: Ready for the United States.

The Court: You may proceed. I am waiting, gentlemen.

Mr. McHale: Very well, your Honor. I believe I am starting my cross-examination now.

The Court: Yes. Mr. Hover, will you take the stand, please?

HERBERT D. HOVER

the plaintiff herein, called as a witness in his own behalf, having been previously sworn, resumed the stand and testified further as follows:

Cross-Examination

By Mr. McHale:

Q. Mr. Hover, you stated you have been in business here——

Mr. Mortenson: Before Mr. McHale starts his cross-examination could I ask one question on a matter that may have been a little confusing? [100]

The Court: Go ahead.

Mr. Mortenson: I think I asked some questions and you did too, your Honor, about the Pavilion Room and the witness, I think, understood that I was asking about the distance back at which you

(Testimony of Herbert D. Hover.)

could observe the floor show. I believe he said something like 16 feet. I am not sure, but he wasn't at that time testifying about the length of the room itself which, of course, shows on the diagram as being much greater than that.

I just wanted to ask whether there was any confusion in the court's mind as to what his testimony was.

The Court: Well, I have now viewed the premises and there is no confusion in my mind.

I think that anybody sitting in the Pavilion Room, quite frankly, could see the floor show if he wanted to.

If they drew the curtain then they couldn't see the floor show, but the curtain was only drawn for the overflow crowds from the lounge and main room. But if the Pavilion Room private party had the accordion doors open anybody could see it if he wanted to see it. He might have to stand or strain his neck, but if a person was in the front part—16 feet or whatever it was Mr. Hover said, you could see it with greater convenience than you could in the rear, but I think as far as I am concerned the record should be clear that anybody could view it from the Pavilion Room with the [101] accordion doors open if they wanted to.

Mr. Mortenson: Provided they stood up in the back part. I sat in the back and I couldn't see the stand myself.

The Court: Frankly there are many main rooms where it is difficult for a patron to see a performer.

(Testimony of Herbert D. Hover.)

It would be more difficult to see the show from the rear I will admit, but it could be seen.

Mr. Mortenson: I have no further questions. Has the original deposition been filed? Well, I assume that since we have the witness here it isn't necessary to file the deposition.

Mr. McHale: I would like to have it filed. Do you have it?

The Court: Yes, I have the original. Why do you want it filed?

Mr. McHale: I simply want it available.

The Court: Hand this to counsel.

Mr. Mortenson: He has a copy of it.

The Court: You want to use it for purposes of impeachment?

Mr. McHale: Yes.

Mr. Mortenson: I just didn't see the point in filing the deposition.

Mr. McHale: Just so we have the original available.

Mr. Mortenson: Yes. And it is signed. There are five [102] typographical errors—well, some five minor corrections. Aside from that it is signed and notarized.

Q. (By Mr. McHale): Mr. Hover, you testified yesterday regarding the Pavilion Room. I would like to know first of all what the basis of your testimony is as to the number of people who stayed to see the floor show of the Pavilion Room parties. Now, as I understand it, there were at least 304 parties during that period.

(Testimony of Herbert D. Hover.)

Do you have any records that would show you or would indicate how many people in those parties stayed to see the main room floor show?

A. No, sir, we do not.

Q. Then I suppose your answer would be that you have no records that would show what people went home before the floor show started?

A. Only my own observation and what I recall.

Q. But you have no records?

A. We never were required to keep records, counselor. The Treasury Department knew what we were doing. They okayed it. We were not required to keep records. We kept records of everything we were required to keep.

Mr. McHale: I move to strike the answer of the witness.

The Court: I will let it stand.

Mr. McHale: The records that you have of the sales in [103] the Pavilion Room are broken down, are they not, into sales of food and sales of beverages, is that correct? A. Yes, sir.

Q. Except for the total for each evening is there any other record of those sales that you can tell from what time any of the sales were made or the time when drinks were dispensed from your present records? A. Yes, sir.

Q. You can? A. Yes, sir.

Q. What do you have so you can tell that?

A. Well, we can tell from 10:30 on when the price of things changed.

(Testimony of Herbert D. Hover.)

We know that all drinks that were charged at 90 cents started at 9:30.

Q. Well, did you in your bookkeeping records enter in a different column or in some way that you could tell the number of drinks that were sold at 90 cents and the number sold at 75 cents? Is there some way you can distinguish that?

A. Yes, from the tapes of the register.

Q. You have the tapes?

A. I believe we do. I haven't seen them but I believe we do.

Q. Have you looked for them? [104]

A. No, sir, I have not but we keep our records for the required period of time. I am sure we have them.

Q. Where would they be—at the restaurant?

A. Yes, sir.

Q. You wouldn't have any records that would indicate the number of people who were present at these Pavilion Room parties, who either left before the show started or stayed afterwards, and similarly I suppose you would have no records to show when the people left—I mean you wouldn't be able to tell from the records you have at what time the people actually left, whether it was 11:30 or 12:00 or 12:30 or 1:00 o'clock? A. No, sir, we do not.

Q. Do you have any records by which you can tell with respect to any evening in this period in which the Pavilion Room was open, how late the bartender stayed on duty in the Pavilion Room?

A. No, sir, we do not.

(Testimony of Herbert D. Hover.)

The Court: Can you tell me how you arrived at the figure of 90 cents for drinks at 10:30 instead of 75? Why exactly a 15 cent boost? Was there a particular reason for that, Mr. Hover?

The Witness: Well, originally we used to charge 75 cents for what we called bar brands and 90 cents for de luxe brands and when it was necessary to increase—to make a [105] change we kept it at 90 cents. It was much easier for the customer instead of making it 85 or 95 cents.

Now why we made it at 10:30, sir, this goes back——

The Court: You explained that in your direct examination. You said it was because of the extra bartender.

The Witness: We took the same figure as we charged for de luxe brands. In other words, it made it a less complicated contract. It was easier for a man booking a party to absorb certain costs.

The Court: The reason I asked the question, quite candidly, is because the Government suggests in its brief that the boost from 75 cents to 90 cents is exactly 20 per cent.

The Witness: There may have been, sir. It goes back many years. I don't know, sir. That may have been it initially—why it was done.

The Court: All right, you may continue.

Mr. McHale: Will you mark this please, Mr. Clerk?

The Clerk: Defendant's Exhibit A marked for identification.

(Testimony of Herbert D. Hover.)

(The exhibit referred to was marked Defendant's Exhibit A for identification.)

Mr. McHale: I offer at this time as Defendant's Exhibit A, your Honor, a summary of the Ciroette Room records, which is similar to that—I mean based on the same principle as [106] Exhibit 2, Plaintiff's Exhibit 2.

Mr. Mortenson: No objection.

The Court: Received.

(The exhibit referred to, marked Defendant's Exhibit A, was received in evidence.)

Mr. McHale: Would the clerk hand the exhibit to Mr. Hover, please?

(Document handed to the witness.)

Mr. McHale: And would the clerk hand Exhibit 2 to Mr. Hover, please?

(Document handed to the witness.)

Q. (By Mr. McHale): Mr. Hover, you testified yesterday that one of the reasons you raised the drink prices at show time was the necessity of keeping an extra bartender on duty in the Pavilion Room.

Now, wouldn't the same principle be applicable to the Ciroette Room?

A. Not necessarily. It may be. It all depends on the circumstances, but not necessarily. One would not necessarily follow from the other.

Q. Well, did you keep a bartender in the Ciroette

(Testimony of Herbert D. Hover.)

Room? You had a bar up there. You had a bartender up there, is that correct?

A. At certain times. Maybe for an hour or half hour or all night. Pardon me. I didn't understand your question. [107] Do you mean do we keep a bartender there all night whenever there was a party?

Q. Yes.

A. The answer to that would be no, not all night sir.

Q. Well, at what time would you pull the bartender out of the Ciroette Room?

A. That would depend upon the requirements of each individual party. Some parties required no bartenders. Some parties said: "We will drink only for a half hour, from 5:30 until 6:00." And some said: "We want him there all night."

Sometimes we didn't keep a man there all night even though requested for all night because it was economically not feasible to do so.

Q. There were parties in the Ciroette Room when the bartender was kept all night, is that correct?

A. I don't know. There may have been. There may have been. I don't know.

Q. Well, I invite your attention to Defendant's Exhibit A, the summary regarding the Pavilion Room. You will notice there is a column headed "Cost Per Person" of the drink on the right-hand side? A. Yes, sir.

Q. Do you find that column?

A. On Exhibit A that applies to the Ciroette Room. [108]

(Testimony of Herbert D. Hover.)

Q. Explain the column.

A. You will note the drink price almost without exception is 75 cents.

Q. Yes.

A. Whereas the Pavilion Room is 75 cents and 90 cents most of the time.

Q. Yes.

A. Except for the very beginning. What is the question?

Q. How do you explain the fact—how do you explain your reasoning in saying that you needed an increase in price in the Pavilion Room in order to have a bartender when you never needed an increase in price to have a bartender in the Ciroette Room?

A. Well, the parties in the Ciroette Room were invariably much smaller than the parties in the Pavilion Room and usually it was necessary to have a bartender there for a very limited time. We would double the bartender from downstairs.

The parties in the Pavilion Room were the larger parties and there may have been more requirement for a bartender. But speaking generally, there is no general rule. Each party is handled on its own, basically, except the parties in the Ciroette Room were smaller and the price of the same food was even lower in the Ciroette Room than [109] in the Pavilion Room.

The Court: I think the question is, why would the price go to 90 cents if you didn't supply an additional bartender which, I think you gave as the

(Testimony of Herbert D. Hover.)

reason why you had to boost the prices to 90 cents. That was because you had to put a bartender on for all night.

The Witness: Yes.

The Court: Why would you increase the price when you didn't put a bartender on?

The Witness: I don't think I understand that, sir. Why we would increase the price?

The Court: If anyone stayed after 10:30——

The Witness: If anyone stayed after 10:30 we would have to have a bartender there all night.

The Court: In every instance you put a bartender in the room if they stayed after 10:30?

The Witness: Yes, sir, because we couldn't double a man from the front bar—the service bar in the Pavilion Room if they stayed after 10:30.

The Court: Could you use that lounge bar there which is so close to the Pavilion Room?

The Witness: No, sir.

The Court: Why?

The Witness: That was open to the public. The Pavilion Room was not open to the public. There were two different [110] operations. One was a closed house and the other was open to the public. But as I said before this goes back many years. I think that was it—why we did it.

I couldn't testify truthfully now why we made certain decisions in 1951—six years ago.

Q. (By Mr. McHale): It is true, is it not, Mr. Hover, with respect to the Pavilion Room, that the increase in price was invaribly 20 per cent or from

(Testimony of Herbert D. Hover.)

75 cents to 90 cents? A. Yes, sir.

Q. It never varied? A. Yes, sir.

Mr. Mortenson: May I call to the court's attention a mathematical error that is being committed here.

If a drink is 90 cents, 20 per cent of that is 18 cents according to my computation.

The Court: If the drink is 75 cents and you boost it to 90 cents that is a 20 per cent boost.

Mr. Mortenson: But that isn't the way it works. If you have a drink that sells for 90 cents you pay a cabaret tax on that of 18 cents.

The Court: We are not talking about that. Just a moment. Hear me out. If a drink sells for 75 cents and it goes to 90 cents that is a 20 per cent boost.

Mr. Mortenson: Yes, but it has nothing—— [111]

The Court: That is the point they make. That is the point they make as I take it.

Now, I am not ready to agree with it but the inference they want me to draw is that they boosted it exactly 20 per cent. I understand the point you make.

Mr. Mortenson: Well, if they were going to absorb 20 per cent more cabaret tax they would have to make it 95 cents because then it would be 76 cents left.

The Court: All right.

Mr. McHale: That is a matter of argument.

Mr. Mortenson: I think it is a matter of mathematics.

Q. (By Mr. McHale): With respect to the bar

(Testimony of Herbert D. Hover.)

in the Pavillion Room, that was a profitable operation, wasn't it, Mr. Hover?

A. Well, do you mean that single operation? I don't quite understand your question.

Q. What I mean to say is, you made a bigger profit out of the sale of the drinks than you did out of the sale of food, didn't you?

A. I can't answer that categorically. It would seem the answer would be yes. I don't wish to be caustic about it, but sometimes you didn't—sometimes you made more on food. It all depends on how many drinks you serve.

Q. Over the long run, in the general run of this period involved, wasn't it pretty cheap an investment to [112] put a bartender in the Pavillion Room to sell those drinks to those people you have got in there at these private parties?

A. It all depended. We had other costs involved. I would normally—I might say yes—I might say yes but there are many exceptions to it.

Q. Now, you previously testified that you have no records that would show you what number of people stayed for any particular party to witness the entertainment.

Now, we know that during this period there were at least 304 parties. We know that you have folders for those 304 parties. That is the basis on which Exhibit 2 was made up.

Now, are there any of those 304 parties at which you specifically say that nobody stayed?

A. Yes, sir.

(Testimony of Herbert D. Hover.)

Q. All right. Will you please tell us which parties they are by referring to Exhibit 2? And I am talking about the Pavilion Room.

A. Pavilion Room?

Q. Yes, that is Exhibit 2.

A. I do not recognize any by name, sir.

Q. All right. Are there any of those parties where you say that any specific percentage stayed or didn't stay or went home before the floor show started? A. I cannot say, sir. [113]

Q. Are there any of those specific parties in which you can say the curtain was not drawn—that is, the group did not see the floor show?

A. You are talking about specific parties?

Q. Yes. A. No, sir; I cannot say.

Q. We have here in the courtroom, Mr. Hover, your files, folders regarding these parties. They are available here if you wish to refresh your recollection. Would they help you any?

A. No, sir; those contracts are written before the parties, weren't they?

Q. Yes.

A. Those contracts have no bearing of what occurred on the night of the party—that is, whether the curtain was drawn.

Q. Would you not be able to refresh your recollection?

A. There is nothing there to refresh. I will look at the folders if you wish me to.

Q. Tell me, Mr. Hover, what other regular employees you had with you during most of this pe-

(Testimony of Herbert D. Hover.)

riod—I mean—I don't mean other employees, but what employees did you have during this period?

A. Well, we had——

Q. In one capacity or another—the major ones. I [114] don't mean the bus boys and waiters.

A. In the office we had a manager.

Q. Well, let us forget about the office. The office people would only be there in the daytime?

A. Yes, sir.

Q. Pretty much? A. Yes, sir.

Q. List the people who would be there during the hours of operation in the evening when these Pavilion Room parties were going on.

A. Well, basically the kitchen help, dining room help, musicians and show and the concessionaires.

Q. What individuals were there pretty regularly throughout the period?

A. You mean in the dining room crew?

Q. Yes. I mean, for instance, you must have had a headwaiter and orchestra leader?

A. Yes, sir.

Q. Can you name the major individuals in your staff? A. We had a headwaiter.

Q. What was his name? A. John Oldrate.

Q. He was there during this period?

A. The major portion of it, yes, sir.

Q. Who else? [115]

A. Well, I am trying to get the question. Do you mean on the music or only in the dining room crew?

Q. I mean people who would be around, who

(Testimony of Herbert D. Hover.)

would know what is going on in the Pavilion Room besides yourself?

A. Well, the headwaiter may know.

Q. And that was Oldrate? A. Yes.

Q. Who else?

A. Some of the waiters may know.

Q. Are they still around?

A. Well, the crew has changed pretty much. One or two men may be around.

Q. Who else would know—how about bartenders? Are they pretty regular?

A. Well, we have one bartender now. I don't know whether he worked there during that period or not. He probably did. He probably did. I know he came and left. Bartenders will come and go. I don't know.

Q. What is his name? A. Sammercelli.

Q. And you had one or two, of course, orchestra leaders that were there most of the time, didn't you? A. Yes, sir.

Q. Who were they?

A. Dick Stabile. [116]

Q. And who else?

A. Well, then, we have another band. It might have been—may have been Bobbie Ramos.

Q. These individuals you have named would be around there in the evening and would know what was going on, wouldn't they?

A. They would not. They would be around there in the evening but they wouldn't know what was going on in a party.

(Testimony of Herbert D. Hover.)

Q. But they would more or less see your operation—they would be there most of the time over a period of three or four years?

A. That depends on what you mean by "see our operation." They wouldn't know what went on.

Q. They were there regularly six or seven nights a week throughout this period?

A. I am trying to give you an answer, sir. To tell you the truth an orchestra leader wouldn't have any idea what goes on. He is only interested in music and hangs around backstage.

Q. You had another employee who was in charge of making arrangements for these parties?

A. Yes, sir.

Q. And her name was what?

A. Mrs. Miller. [117]

Q. Dolores Miller?

A. Dolores Miller, yes.

Q. I believe you testified on direct, did you not, that you were your own advertising man—you did your own drafting of ads?

A. Basically, I did, yes.

Q. These advertisements—Exhibits 4-A, 4-B and 4-C. You drafted or had a hand in laying those out, did you?

A. I would assume responsibility for that, sir; yes, sir.

Q. Well, when you put such phrases in those ads that your group will be able to see "our fabulous show at no extra cost" and so forth, what did you intend by that? A. What I intended by it?

(Testimony of Herbert D. Hover.)

Q. Yes.

A. Well, I intended several things. You can come into the main room and see the show. You can also see the show from the Pavilion Room if you so wanted to.

Q. In other words, weren't you, Mr. Hover, offering to the patrons or people who would book the Pavilion Room as an inducement the right to see the floor show?

Mr. Mortenson: I object to the form of that question, your Honor, as to what was an inducement. That is a subjective matter that I don't believe has any place in a tax case. [118]

The Court: Objection overruled.

The Witness: May I have the question?

Mr. McHale: Will you read the question?

(Question read.)

The Witness: Well, I wouldn't necessarily say it was an inducement, but it was one of the features which—under some circumstances you could see the floorshow.

Q. (By Mr. McHale): Mr. Hover, the addition or the construction of the Pavilion Room was done under your period of ownership, was it not?

A. Yes, sir.

Q. It was your idea the building of the Pavilion Room, was it not? A. Yes, sir.

Q. And this idea of having a low wall with an accordion curtain or folding wall, that was your idea, was it not?

(Testimony of Herbert D. Hover.)

A. Well, it was a result of conferences with an architect, but I would assume responsibility for that, sir.

Q. Mr. Hover, there were several occasions or many occasions, were there not, when you didn't have these, what you term "private parties" in the Pavilion Room and the Pavilion Room would be dark for that evening, but if you had a major attraction and the regular part of your main room and lounge would be booked solid, you would use part of the Pavilion Room as part of your main cabaret operation? [119]

A. We would try to do it, yes, the front portion.

Q. You used the front portion?

A. Yes, sir.

Q. And that happened many times, didn't it?

A. A number of times.

Q. On New Year's Eve it was a standard practice to use all of your Pavilion Room as part of your main operation? A. No, sir.

Q. It wasn't? A. No, sir.

Q. Did you usually have a separate party on New Year's Eve?

A. No, sir. We never went beyond two rows of tables.

Q. Then your testimony with respect to New Year's Eve would be the same as with respect to a major attraction?

A. If people would sit there we would—we would have difficulty seating people there but we never went beyond two rows of tables in that room.

(Testimony of Herbert D. Hover.)

Mr. McHale: At this time, your Honor, I would like to, if it is agreeable with counsel here, to break the cross-examination of Mr. Hover. I have some witnesses subpoenaed to testify about the Pavilion Room and if I could resume with Mr. Hover at a later time I would appreciate it. I would like to call these witnesses out of order as part of the Government's case. [120]

Mr. Mortenson: I have no objection.

The Court: I would prefer that you finish the cross-examination.

Mr. McHale: All right. This is my thought, your Honor. One of the features of the case is a closed house. That is completely different—not completely but it is considerably different than the Pavilion Room in itself. Most of the rest of my cross-examination will be based on the closed house arrangement.

The Court: How about the Ciroette Room? Do you have any further cross-examination on that?

Mr. McHale: Yes, a couple of matters with reference to the Ciroette Room.

Q. (By Mr. McHale): Mr. Hover, it was your practice—we have stipulated that five per cent of the receipts of the Ciroette Room represented people who were taken down to see the floor show from the Ciroette Room. In other words, we realize you couldn't see the floor show or hear the orchestra up in the Ciroette Room, but five per cent were taken down to see it.

Now, my question is did you make any charge

(Testimony of Herbert D. Hover.)

for that, any additional charge like a cover charge or admission charge for that?

A. You mean the people that went down from the Ciroette Room downstairs? [121]

Q. That is right.

A. I would say there may have been some instances there was a cover charge. It would depend upon where they sat. If they sat in the no cover charge part of the room then there was no cover charge.

Q. I understand your normal practice was to put them in the back of the lounge or the first two rows of the Pavilion Room. Did you make a charge there?

A. If they consumed anything we did.

Q. Did you charge them, not for their food and drink, but a special charge for bringing them down —an admission or cover charge?

A. There was no cover charge or admission charge where they sat.

Q. You made no additional charge for that privilege?

A. If they sat where we charged a cover charge they paid. If there was no cover charge there was no payment.

You can walk in off of the street. It is the cheapest place in town. You can walk in off the street and not spend a dime. Anybody can do that. And if anybody sat there in a no cover charge place they didn't pay anything. There never was any admission.

(Testimony of Herbert D. Hover.)

They had a right to do the same as anyone else in the United States. But if they sat in a cover charge part of the room they were charged a cover charge. [122]

Q. We understand that. Now, with respect to the Pavilion Room. You made no extra charge or additional charge for the people to sit in the Pavilion Room when you opened the sliding curtain so they could see the floor show?

A. No, sir, we did not—no, no extra charge.

Mr. McHale: That will be all at this time, your Honor, on that phase of the case. He is your witness, Mr. Mortenson.

The Court: Just a moment. May I see those ads, please?

(Documents handed to the court.)

The Court: When you had this phrase in your advertisement: "Arrangements can be made for your group to see our fabulous floor shows and dancing at no extra cost," you were holding out to the public the fact that they could see the show and dance without paying the 20 per cent tax, isn't that in effect what you were doing?

The Witness: No, sir. We did one of two things——

The Court: Go ahead.

The Witness: You could have your party in the main room and pay a tax, which happened very often, or if you held your party in the Pavilion Room—if you had a private party from 6:00 until 10:00 it was possible to see the show.

(Testimony of Herbert D. Hover.)

That was a ruling we had from the Treasury Department. They checked our contracts. They knew what we were doing. We were aboveboard in every instance. We conformed 100 per cent with what the men in the Treasury Department permitted [123] us to do. And we had no right to deprive any man because, if he wanted a private party in the Pavilion Room, to deprive him of the same rights another man had who walked in off of the street to sit down in a lounge in a certain part of the room and see the show. We had definite rulings on that.

The Court: Just a moment. A man who came in from the outside and had a drink at the bar or the lounge didn't pay any cover charge, is that correct?

The Witness: Ordinarily he didn't. Or he can sit in certain parts of the room and there is no cover charge.

The Court: What happened to a man who came in, let us say at 10:30, when the show went on and sat in the lounge, just had a drink there and watched the show and didn't pay any charge?

The Witness: He didn't have to have a drink. We didn't even solicit drinks.

The Court: Do you mean to tell me——

The Witness: We didn't do any of those things. That is why we went broke. I wish we had now.

The Court: You mean you invited the public in to watch that show without having a drink?

The Witness: Sir, on your average you will sell two drinks to a person anyway and it is seldom you

(Testimony of Herbert D. Hover.)

will get four people in who will sit all night without having drinks. The bartenders complained that the bar was cluttered up with [124] people who didn't buy a drink at all.

The best attraction we ever had was Johnny Ray, who is married to my competitor's daughter. He played at Ciro's because he knew when he came into Ciro's he didn't have to spend five cents. Nobody bothered him. And he said, "If I ever become famous I will stay with Ciro's."

He married my competitor's daughter and we came out ahead in the long run. We never solicited any drinks. It is the cheapest place in town.

Whatever we did, we did not feel that we had a right to penalize anybody because they attended a private party and in a private room—we did not feel we had a right to penalize them and withdraw certain privileges from them that were open to everyone—to every member of the public.

We openly advertised it. The Treasury Department knew about it. The revenue agents checked it. They attended parties. Everything was done open and aboveboard and whatever taxes we had to collect we collected and we paid it. It was difficult at times but we paid it.

The Court: All right, go ahead.

Mr. Mortenson: Shall I save my redirect examination?

The Court: Suit yourself. Maybe you ought to do it on this point.

(Testimony of Herbert D. Hover.)

Mr. Mortenson: I just have a couple of questions with regard to this matter of cover charge and sales of liquor [125] during the show time.

Redirect Examination

By Mr. Mortenson:

Q. Did you have any special arrangements with groups like the Arthur Murray dance studio, for instance?

A. We had many arrangements, yes. If you are referring specifically to the Arthur Murray group, they would come in. There would be no cover charge. They were guaranteed like two drinks per person or sometimes chicken a la king—a cheap deal as far as we were concerned, but it helped fill the room and we were glad to have those deals and we solicited those deals and some of this advertising was used to solicit those deals, yes, sir.

Mr. Mortenson: That is all I have.

Recross-Examination

By Mr. McHale:

Q. Mr. Hover, you have no written rules from the Treasury Department on your cabaret?

A. The Treasury Department will not give you a written ruling. If they did it wouldn't even be effective. I wish they had given me a written ruling and I wish they were bound by it because all my problems would be over. They had rules. They audited our books. They said we were doing [126]

(Testimony of Herbert D. Hover.)

okay. We advertised openly. We did nothing underhand.

The Court: May I suggest your problem wouldn't be over because you would still have the problem of the free drinks given out at the bar.

The Witness: Free drinks?

The Court: I should say the people who came in and don't drink at all which you said was a problem.

The Witness: We averaged two drinks per person.

Mr. Mortenson: They are freeloaders—they are different.

The Witness: And you have your tourists and they don't drink at all.

The Court: All right, go ahead.

The Witness: We also did—we were respected the same as any place in the United States in the enforcement of the cabaret tax. I studied this thing in Las Vegas and New York and Chicago and Florida and Washington. We enforced the cabaret tax stricter than any place in the United States, including places within throwing distance of Ciro's and we had nothing but complaints because people thought we were discriminating—they thought we were keeping the cabaret tax.

I wish to God Ciro's was permitted to operate the same as every other place in the United States is permitted to operate. [127]

Mr. McHale: I move to strike that.

The Witness: It is true, sir, it is true.

The Court: You are going to be excused for the time being.

Mr. McHale: I would like to call Mr. Johnson out of order, if I may.

Mr. Mortenson: Certainly.

VINCENT JOHNSON

called as a witness on behalf of the defendant, being first sworn, was examined and testified as follows:

The Clerk: State your full name.

The Witness: Vincent Johnson.

Direct Examination

By Mr. McHale:

Q. What is your occupation, Mr. Johnson?

A. I am office manager for a building contractor.

Q. And in 1954 were you a member of a group that arranged a party at Ciro's restaurant?

A. Yes.

Q. What was the name of that group?

A. Called the "Engineers-Constructors Society."

Q. And were you the person who made the arrangements for the party? [128] A. Yes.

Q. And was the party held in the Pavilion Room? A. Yes.

Q. And how did you go about arranging it? Did you get in touch with Ciro's by telephone?

A. All the arrangements were made by telephone, yes, sir.

(Testimony of Vincent Johnson.)

Q. Made by telephone. Did you speak to Mr.——

A. To Dolores Miller.

Q. Mrs. Miller was the person who negotiated the party? A. Yes.

Q. You arranged for a party on February 26, 1954, is that correct? A. That is right.

Q. In the Pavilion Room? A. Yes, sir.

Q. And do you have any correspondence or contracts or anything that you entered into with Ciro's?

A. Yes, sir; I have a copy of the agreement.

Q. Did you bring it with you? A. Yes.

Q. May I see it, please?

Mr. McHale: Will you mark this for identification, please?

The Court: Are you going to offer it? [129]

Mr. McHale: Yes.

The Court: Show it to Mr. Mortenson and maybe it can go right into evidence.

(Document handed to Mr. Mortenson.)

Mr. McHale: I offer the February 11, 1954, letter as our next exhibit in order, your Honor.

Mr. Mortenson: No objection.

The Clerk: Defendant's Exhibit B in evidence.

(The exhibit referred to, marked Defendant's Exhibit B, was received in evidence.)

Q. (By Mr. McHale): You were the one who was given the duty of arranging this party for your group, is that correct?

A. That is correct.

(Testimony of Vincent Johnson.)

Q. Did you consider other establishments before you finally decided upon Ciro's? A. Yes, sir.

Q. What others?

A. Well, I recall we checked with the Biltmore Bowl and I believe the restaurant on Sunset Boulevard there just east of Vine Street. I can't recall the name right now.

Q. And was this a party arranged for—was it a mixed group—men and women? A. Yes.

Q. And what arrangements were made with Mrs. Miller with respect to dancing or music or anything of that sort— [130] a floor show?

A. Yes. We were told that we would have our own private room; that we would have our own private bar, our own dance floor and that the music would be furnished from the main stage but it would be wired to the room.

Q. And what were the arrangements with respect to your group seeing the floor show?

A. We were told that at floor show time the curtain would be drawn and we could see the show.

Q. And was that done? A. Yes.

Q. And did your group see the show?

A. Yes, sir.

Q. And what percentage of your group saw the show, would you say?

A. I would say 100 per cent.

The Court: How large was the group?

The Witness: Roughly 85 persons.

Q. (By Mr. McHale): And how long did the party continue?

(Testimony of Vincent Johnson.)

A. I believe the majority of the people were there until midnight.

Q. And was there a bartender in the Pavilion Room? A. Yes, sir.

Q. During that period? A. Yes, sir. [131]

Q. You will notice in this letter of February 11—do you have it in front of you? A. Yes.

Q. There is a paragraph stating in substance that the bar will be open and that drinks will be charged for at the rate of 75 cents per drink until show time at 10:30 and 90 cents per drink thereafter.

Was a reason given to you for that increase in price? A. None that I remember, no.

Q. You don't remember any particular reason?

A. No.

Q. Did you understand that there was a reason for it?

A. Well, I believe everyone assumed that there was the matter of taxation there.

Mr. Mortenson: Pardon me. May I ask that that be stricken, your Honor?

The Court: Yes.

Q. (By Mr. McHale): Was the opportunity to see—what was the floor show at Ciro's?

A. It was the opening night of the Julius LaRosa show.

Q. Was the opportunity to see the floor show one of the reasons that you selected Ciro's?

A. Yes.

Q. It was an inducement? A. Yes. [132]

(Testimony of Vincent Johnson.)

Q. When the floor show went on what did the people in your group do to see the show? Did they remain seated at the tables?

A. No. They rearranged their seating somewhat to get as close to the curtain as possible.

Q. Did people in your group go down and dance on the main room dance floor?

A. Yes; I believe a few did.

Mr. McHale: That is all, Mr. Johnson. Your witness.

Cross-Examination

By Mr. Mortenson:

Q. Mr. Johnson, did you enjoy the show?

A. Very much.

Q. When you called the Biltmore did you ask about a private room?

A. No, sir; we didn't.

Q. Did you have any discussion with the person you talked to at the Biltmore about a cabaret tax?

A. No, sir.

Q. You didn't? A. I don't recall.

Mr. Mortenson: That is all.

The Court: Step down. Would you prefer to take a recess at this point? [133]

Mr. McHale: I think it would be a good opportunity.

The Court: All right, we will have a short recess.

(Short recess.)

The Court: You may proceed.

Mr. McHale: Mr. Frederick Payne.

FREDERICK PAYNE

called as a witness on behalf of the defendant, being first sworn, was examined and testified as follows:

The Clerk: State your full name.

The Witness: Frederick Payne.

Direct Examination

By Mr. McHale:

Q. During 1952 what was your occupation, Mr. Payne?

A. I was assistant manager of the Security-First National Bank in Santa Monica.

Q. And did you arrange for a party—for some group at Ciro's restaurant? A. Yes.

Q. And what was that group?

A. It was the employees of the Security-First National Bank, 14th and Wilshire in Santa Monica.

Q. And do you have any papers or documents or anything with respect to that? [134]

A. No; I don't have a thing in my possession.

Mr. McHale: I offer Ciro's correspondence file regarding this party.

The Clerk: Defendant's Exhibit C for identification.

(The exhibit referred to was marked Defendant's Exhibit C for identification.)

Q. (By Mr. McHale): In that file, Mr. Payne, there is a letter addressed to Fred Payne, dated

(Testimony of Frederick Payne.)

March 14, 1952, and at the foot it is marked "Accepted" and "Approved." Is that your signature?

A. Yes.

Q. That is the contract or arrangement you entered into with Ciro's, is that correct?

A. Right.

Q. With whom did you deal in arranging this party? A. Mrs. Miller.

Q. At Ciro's? A. At Ciro's.

Q. And did you consider other places, restaurants or night clubs or hotels?

A. Yes, sir. Prior to the time we decided on having our party here we talked to the Miramar Hotel in Santa Monica, the Riviera Country Club and I believe also the Santa Ynez Inn in Santa Monica.

Q. But eventually you decided on Ciro's? [135]

Q. And your group—what kind of group was it? Was it a mixed group, men and women?

A. That is right, husbands and wives.

Q. And the date of the party was April 19, 1952, is that correct? A. Yes.

Q. Do you remember what the attraction was on that night—what the floor show was?

A. No; I frankly do not remember.

Q. You don't recall that? A. No.

Q. Your group did see the floor show, is that correct? A. Yes.

Q. When you made this arrangement for the party at Ciro's was it stated that your group would have the opportunity to see the floor show?

(Testimony of Frederick Payne.)

A. Yes; that the accordion wall would be drawn so that we would be able to see the show.

Q. And your party was in what we call the Pavilion Room? A. Yes, sir.

Q. How many people were in your group?

A. Between 55 and 60.

Q. And was there a bartender and bar in that room? A. Yes, sir. [136]

Q. How late was the bar kept open?

A. Well, to the best of my memory I would say about midnight. That is about when the majority of the people left.

Q. And the floor show went on at about 10:30?

A. 10:30.

Q. And the accordion curtains were open at show time so the party could see the floor show?

A. That is right.

Q. And what percentage of the people would you say in your group stayed to see that floor show?

A. Almost 100 per cent.

Q. Was the ability to see the regular Ciro's floor show the reason or the inducement for your group to have its party there?

Mr. Mortenson: I object to the question, your Honor. It calls for a subjective state of mind.

The Court: Well, I will sustain that objection. I think we have had the question pretty much answered by Mr. Hover himself.

Q. (By Mr. McHale): Did some members of your party go into the main room and dance in the main room?

(Testimony of Frederick Payne.)

A. I believe that a few may have.

Q. About what time did the party break up?

A. I would say about midnight.

Mr. McHale: Your witness. [137]

Mr. Mortenson: No cross-examination.

The Court: Step down.

I want to pose this hypothetical question once more to make sure that I am clear on this. It is not to be taken as an indication of any way in which I am going in this case because at this point I frankly do not know. But in the event that I were to find that it is a private party until 10:30 and then becomes a public performance at 10:30 what am I going to do about amounts? Now, that is what worries me. How am I going to apportion this.

Mr. McHale: First of all, your Honor, of course we consider the fact that the law is—that the statute, I think, is quite clear, that the entire amount paid during the evening for any person who is entitled to be there present during the entertainment period is taxable.

The Court: And suppose I don't agree with that?

Mr. McHale: If you don't agree then I think we have a problem in that respect.

The Court: We haven't seen these tapes Mr. Hover talked about. I think we are going to have a great deal of difficulty as to time—what time the payments were made.

Mr. McHale: If your Honor is going to depend on the timing, we have the bar going all evening.

We have the meal completed ordinarily at 10:00 o'clock or so. If such a thing as the mechanics of paying the check is important that [138] would be rather difficult. I do not think that is a good basis upon which to decide a case but——

The Court: I don't necessarily mean the time of paying the check. I quite agree with you there. Is there some way of apportioning the amounts paid for the entire evening?

Mr. Mortenson: Yes, your Honor, there is. There is available records—we think they are available. In the Pavilion bar there is a cash register. Each cash register has its own number so that you can identify a tape taken from a register.

Now, at a point on this register instead of a 75 cent item or a dollar and a half item you will find a 90 cent item or a dollar and eighty cent item and so on. That will determine the hour, 10:30 as we have been talking about here.

The Court: No; you still don't get my point. I understand that, and that is all right. If you want to use the tape that is all right with me but I think you should compile a summary of it because I don't think I should start going through this tape looking for these figures.

But do either of you desire to comment on this, and that is an allocation to be made based upon the number of hours ordinarily consumed by a private party, let us say from 7:00 to 12:00 o'clock, and let us say it cost $5 from 7:00 to 12:00 for a dinner. Would there be an hour and a half that would carry a tax? Do you understand my question? [139]

Mr. McHale: You mean to take the total receipts from the Pavilion Room and divide them by hours?

Mr. Mortenson: Mr. Hover says that is unrealistic. I think everyone in this room is sufficiently sophisticated to know that drinks are generally had mainly before dinner, for one thing, and very few after dinner comparatively.

The hourly basis would be unrealistic. But there is another thing that I don't think has been made clear here.

In the books there is a segregation of what is paid for food and what is paid for liquor. There is no problem about the sale of food after 10:30 so that is completely eliminated.

Then we have only the problem of allocating the charges for liquor after 10:30 and that can be done with exactitude if we have all the tapes because the only place the liquor was sold on which the 20 per cent was not collected and paid over was in the Pavilion Room. It can be done down to the exact dollar if all these tapes are available.

Now, if they are not available we could still come to a very close approximation——

The Court: Let me ask you something, Mr. McHale. Have you ever raised any point concerning the charges in the bar after 10:30? In short, have you ever raised the point that there should be a 20 per cent tax added to that?

Mr. McHale: You mean in the lounge?

The Court: Lounge. [140]

Mr. McHale: I think there has been some con-

fusion. I am going to bring—I thought I would bring Mr. Hover back—I am glad your Honor caught that. I think the evidence is clear that there is a tax on the lounge sales after show time and in fact before show time.

Mr. Mortenson: My understanding is——

Mr. McHale: That is the lounge is always taxable. I think there was some confusion there.

The Court: Always a 20 per cent tax?

Mr. McHale: A half hour before show time.

Mr. Mortenson: I think there is only one——

Mr. McHale: Dancing time—not the show time, so it is earlier than that.

The Court: Is it your contention there is a 20 per cent tax put on the bar checks or lounge checks?

Mr. McHale: Yes, your Honor.

Mr. Mortenson: Well, this is my understanding. Very few people came in early to Ciro's, say at 6:00 o'clock, and the 94 per cent has taken care of that. The six per cent was the non-taxed charges early in the evening.

The Court: That is in the main room.

Mr. Mortenson: The lounge as well as the main room—the main room and the lounge.

The Court: I asked a simple question, if you have the answer and, of course, I want it by testimony. [141]

A man walks into the lounge at 9:00 o'clock and he has some drinks and he doesn't eat and he stays on and he drinks at the bar. Is there a 20 per cent tax on that?

Mr. Mortenson: Yes, sir, and there has been no dispute over that so far as I know.

The Court: Well, then, why shouldn't there be—again don't take by the form of my question that I am urging that there should be—why shouldn't there be at least the same reasoning applied to the Pavilion Room, which is just adjacent to the lounge when you open up those curtains?

Mr. Mortenson: Well, the issue has never been raised because the assessment wasn't set up that way.

The Court: In other words——

Mr. Mortenson: Maybe I should have done it, but I didn't. I took the issues the way they were set up here and, of course, my contention was that it was a private party from beginning to end so I didn't have to cut it off. I am going to now, however, find some way of doing that. But my position was that it was a private party from beginning to end and taxable at no time.

The Court: You see I want to get away as much as possible from labels.

Now, the mere labeling of a private party is not decisive of the issue. You have to go to basic things.

Now, from my observation of the operation of the place, [142] the layout of the place, you have a lounge which is immediately contiguous to this Pavilion Room, so much so that it almost forms one room when you open up those curtains. And what I am concerned with is this, that here is a lounge where 20 per cent tax is placed upon the check. The theory, and it never was contested by the taxpayer,

the theory being that this is a public performance for profit which these patrons are witnessing.

Mr. Mortenson: That is right.

The Court: Now, let us forget the label for a moment. Is there any difference between what the lounge customers are seeing and what the Pavilion customers are seeing when you open the curtain?

Mr. Mortenson: No difference except, of course——

The Court: Then in order to be consistent should you not be urging that there should not be a 20 per cent tax placed on the lounge customers?

Mr. Mortenson: No.

The Court: Why? Forget the label.

Mr. Mortenson: I will forget the label and stick with the basic facts.

We go back to the public performance. Now, the Sigma Chi are having a party with nobody in the party but Sigma Chis and their wives.

The Court: Yes. [143]

Mr. Mortenson: I say that isn't public. It certainly isn't public at the beginning and it isn't public at the time the curtain goes up.

Now, as I tried to point out in my last brief, it seems to me that the Government has confused this matter of what is public with what is private by then saying this: When the curtain opens up the mere fact that the Sigma Chis can look across a room wherein there are people——

The Court: Not only that but can walk down and mingle with them and dance with them on the floor.

Mr. Mortenson: That, of course, makes it difficult, I will admit, because then there is an intermingling. And to that extent my argument isn't so strong, but does that contaminate the entire party —does that make the Sigma Chi party a public party when they sit there and have been there all evening—I am speaking of those who don't go down and dance.

The Court: Well, the query is: Doesn't it make the public, when the management says, "Now, you can come on down here—this is a privilege we are extending to you," is there any difference between that and the Sigma Chis taking a part of the main room, let us say, and the other part of the room being open to the public? Actually what is the difference?

Mr. Mortenson: Then we get into the eternal thing that [144] troubles lawyers and judges: When do you have a change of species or when do you just have different colors? When do degrees create new situations? And you can extend that, I think, to a point where you would say, "Well, sure, it is all public. You open the wall and people mill around back and forth and so it is all a public place."

The Court: Isn't that what the management intends? Doesn't the management intend and hold that out to them and say, "Here, you can be private and as private as you want to be, but remember you can also be public and we can help you be public and we can open these curtains and give you the facilities of the place and mingle with everybody."

Mr. Mortenson: But the public doesn't come in with the Sigma Chis.

The Court: Nobody is going to throw them out if they want to come in there just because the curtains are open from that point on, and from that point on the privacy which the Sigma Chis wanted ceases.

Mr. Mortenson: Well, of course, I can't fail but to see the logic of your position.

The Court: I am not taking a position. I just wanted to throw it out to you because I do this frequently and if I am on the wrong tactic I want to be put on the right one.

Mr. Mortenson: But here is the viciousness of the whole thing. The Commissioner comes out with a regulation. [145] It has never been judicially examined but there it is. What does the regulation say? If anyone is entitled to be present at a public performance for profit in a cabaret the 20 per cent tax applies to all charges if he came in for breakfast——

The Court: Yes, I know that. That is troubling me.

Mr. Mortenson: So you stretch your logic on the other thing and what kind of result do you get? You get a perfectly ridiculous result.

The Court: All right, go ahead.

Mr. McHale: Mr. McGinley, will you take the stand?

FRANCIS V. McGINLEY

called as a witness on behalf of the defendant, being first sworn, was examined and testified as follows:

The Clerk: State your full name.

The Witness: Francis V. McGinley.

Direct Examination

By Mr. McHale:

Q. Mr. McGinley, what is your occupation?

A. I am a welder engineer salesmanager.

Q. And in 1952 did you represent some group that made arrangements for a party at Ciro's?

A. Yes, I did. [146]

Q. And what was that group?

A. Kiwanis Club of Vernon and Southeast Los Angeles.

Q. And did you have any paper or letter or a memorandum by which you entered into a contract at that time with Ciro's?

A. We had a contract. I couldn't find it. However, I do have a copy of our bulletin and the check that I paid the bill with.

Mr. McHale: I offer as Government's next in order Ciro's file on the Vernon Kiwanis party of January 11, 1952.

The Clerk: Defendant's Exhibit D for identification.

(The exhibit referred to was marked Defendant's Exhibit D for identification.)

Mr. Mortenson: Your Honor, we haven't any objection if he wants to offer any further of these

(Testimony of Francis V. McGinley.)

except the folder. There are some doodles and other things on the folder.

The Court: Take out the doodles. We don't want any doodles in the record.

Mr. McHale: In this file there are several letters but particularly there is one on white copy paper dated January 2, 1952.

Q. (By Mr. McHale): Is that your signature?

A. Yes, sir.

Q. That is the agreement that you accepted and approved, is that correct? [147]

A. Yes, sir.

Q. With whom did you make the arrangements for the party, Mr. McGinley?

A. With Dolores Miller.

Q. This letter was dated January 7th, your party was for the 11th, just a few days following that. The party was to be held in what room?

A. In the Pavilion Room.

Q. That is the one with the sliding accordion curtain or wall? A. That is right.

Q. Do you recall what attraction there was on the night you had your party?

A. Yes. It was one of my favorites, Les Paul and Mary Ford.

Q. Was it a mixed group? A. Yes, it was.

Q. Husbands and wives?

A. Husbands and wives.

Q. How many in the party?

A. As I recall, there were about 112.

(Testimony of Francis V. McGinley.)

Q. Were arrangements made for dancing in the Pavilion Room?

A. Yes, we had a dance floor in the Pavilion Room laid down. [148]

Q. With music piped in?

A. That is right.

Q. Were arrangements made in advance? Did you arrange with Miss Miller that the accordion curtain would be open so your group could see the floor show? A. At 10:00 o'clock.

Q. And that was done? A. Yes.

Q. What percentage of your party stayed to see the floor show?

A. I believe most of them stayed.

Q. Was there a bartender at the bar in the Pavilion Room?

A. No, we don't drink at our meetings. We had a cocktail party ahead of it and we had a bartender just before that portion started. We didn't have a bartender after that.

The Court: I take it what was important to you and your members was the attraction that was appearing there, Les Paul and Mary Ford?

The Witness: Well, it was the price and the service, too, along with it. At that time it was pretty hard to get good food and a lot of favors. Of course is was an attraction, I feel, to go to Ciro's, and we did have the best food and the best service. [149]

Q. (By Mr. McHale): I understand at this party you made the arrangements for the dinner, is that correct?

(Testimony of Francis V. McGinley.)

A. Yes. I didn't intend to but some of them were a little slow paying so I paid the check.

Q. What time of the evening did you pay for the dinners?

A. As I recall, it was right after the show was over.

Q. After the show was over?

A. Yes, to Mr. Johnny Andrate.

Q. Mr. Andrate was the one you paid?

A. Yes.

Q. Have you brought the check with you?

A. Yes, sir, I have.

The Court: You paid the entire bill, I take it, after the show was over?

The Witness: Yes, sir.

The Court: What time did you leave that night?

The Witness: I left about whatever time the show was over. I would imagine about a quarter to 11:00.

Q. (By Mr. McHale): Would you say that the entire party departed after the show was over?

A. I would say that probably 90 per cent of them did. Some of them stayed and they went down and took tables and they were on their own from then. I paid only for the meals [150] and the drinks that anyone had were on their own.

Q. Some of the people went into the main room and danced, or went down to the lounge and sat, did they? A. Yes.

Mr. McHale: I offer the check as Government's Exhibit next in order, your Honor.

(Testimony of Francis V. McGinley.)

Mr. Mortenson: No objection.

The Clerk: Defendant's Exhibit E admitted in evidence.

(The exhibit referred to, marked Defendant's Exhibit E, was received in evidence.)

Q. (By Mr. McHale): Before you selected Ciro's you looked into the possibility of having a party at a number of other establishments?

A. Yes.

Q. What were they?

A. At the Biltmore, the Verdugo Club in Glendale, the Oakmont Country Club, and quite a few others.

Q. What was the particular reason why you chose Ciro's?

A. I think one of our other groups had had a party there earlier and they recommended it, plus the fact that the price was attractive, and I think Dolores Miller was a very fine saleslady, and we did have very good service. We had lots of waiters and we wanted to get our meeting on early and through and we were furnished lots of help there. [151]

Q. And the floor show? A. That is right.

Mr. McHale: That is all. Thank you.

Mr. Mortenson: No cross-examination.

The Court: You are excused.

(Witness excused.)

Mr. McHale: Mr. Westengard, please.

JAMES R. WESTENGARD

called as a witness by and on behalf of the defendant, being first sworn, was examined and testified as follows:

The Clerk: How do you spell your last name?

The Witness: W-e-s-t-e-n-g-a-r-d.

Direct Examination

By Mr. McHale:

Q. In January of 1953, Mr. Westengard, what organization did you work for?

A. I was with the Security-First National Bank.

Q. Did you organize a party at Ciro's restaurant?

A. Yes. That was for the Lion's Club, Rancho Park Lion's Club.

Q. With whom did you deal at the restaurant?

A. Miss Dolores Miller.

Q. Do you happen to have a copy of the contract or [152] letter? A. No, I don't.

The Court: How many such witnesses are you going to call?

Mr. McHale: I have two more present in the courtroom. I had a total of nine at the Pavillion Room, some of which are on call.

Mr. Mortenson: I will stipulate that the further witnesses subpoenaed will testify substantially as these witnesses have testified.

The Court: Very well. Why couldn't we get that stipulation and then you can read their names and then a stipulation that if called they would so testify,

(Testimony of James R. Westengard.)

and you can frame your stipulation. You can frame it over the lunch time, if you want to.

Mr. Mortenson: I will go further than that, that whatever contracts are involved I will stipulate to those two.

The Court: All right. Wouldn't that be satisfactory?

Mr. McHale: I think it will be, your Honor. May I just check one contract? I want to be sure about one thing.

The Court: If there is something that is slightly different, that is another proposition, but if they are just going to testify to the arrangements made in advance and what happened after they got there, and the opportunity to see the show and the opportunity to dance, and if they are all the [154] same there is no necessity to repeat their testimony constantly if you can frame it in a stipulation.

Mr. McHale: May I just check one thing, your Honor?

The Court: You could do that over the lunch time. You don't have to do that right now.

Mr. McHale: There is one witness that I might want to call. I just want to check one thing that he might want to testify to.

The Court: Why don't we call that witness anyway.

Mr. McHale: I have forgotten which one it was. I am trying to find it in my papers. I discovered that this morning.

I would like to call Mr. Marvin Stevens.

(Testimony of James R. Westengard.)

The Court: Then I take it as to Mr. Westengard that we will have a stipulation after the lunch hour as to his testimony, is that correct?

Mr. McHale: Maybe we could stipulate now.

The Court: Go on.

Mr. McHale: That with the exception of Mr. Stevens, whom we are going to call now, that all the others, that the testimony that the other witnesses who have been subpoenaed——

The Court: Or will this pertain to the 304 contracts?

Mr. McHale: To the 304 contracts. [154]

Mr. Mortenson: Of course we have this situation, I don't think the agents have interviewed all of the 304. How selective they were in picking the ones they did interview, I don't know. I would assume they wouldn't take the ones they thought were the worst for the Government's side.

Now as far as arrangements and the character of the parties, there is no problem about a stipulation there. The only thing is I wouldn't want my stipulation to cover the percentages of people who stayed because up to now we have one testifying on 100 per cent and one to about 95 per cent, and one to something else. That is something of course that your Honor is going to decide anyway on the basis of all of the evidence and not just on this testimony.

What I am trying to do is shorten this so that we don't have purely cumulative evidence coming in.

The Court: If you are going to shorten it then it is going to have to be a stipulation that is going

(Testimony of James R. Westengard.)

to shorten it. If it is going to leave it open with many questions undecided in the stipulation which he could probably elicit by questioning, then you are going to have to go ahead with it.

I will ask you a couple of questions and see if we can get a stipulation on this from both sides.

No. 1: Are you ready, both sides, to stipulate that the Government was prepared to call—how many witnesses? [155]

Mr. McHale: We originally subpoenaed 10 but I was going to call as many as necessary to establish that most of the people stayed to see the floor show.

The Court: I see. What I was going to try to get at was that you were subpoenaing witnesses who would represent a cross section of the 304 parties. Do we have any agreement on that?

Mr. Mortenson: No, your Honor.

The Court: Then you go ahead and subpoena them.

Mr. McHale: I am willing to do this, your Honor——

The Court: If I am going to draw any inferences, which I take it you want me to draw, that these witnesses are typical of the parties that were run in that Pavilion Room, then I must have something before me from which I can draw that inference.

Mr. McHale: I am willing to do this, I offer this to counsel: May we take at random through this sheet 10 more, and I will go out and subpoena them.

The Court: I think maybe that is the way to do

(Testimony of James R. Westengard.)

it so then I would have some basis to say that these are spot selections and therefore would be typical. That is going to be something you perhaps would want to talk over.

Mr. Mortenson: We might have a practical problem, a time problem in finding them.

Mr. McHale: We can subpoena them for next Thursday [156] morning. I understand the court will still be here.

The Court: Yes. I think that you ought to work it out by stipulation if you can. I don't want to influence you, but in order to save time I think you ought to be ready to stipulate that this was typical.

Mr. Mortenson: I think we can get together on something. This matter of what is typical and what isn't is going to be pretty difficult with this many parties here.

The Court: I think it is pretty well established that there was a pattern, and I really think you ought to stop quibbling and we ought to be able to go to the main point, that there was a pattern, that these people came in, they rented the room at a certain hour, they could see the show if they wanted to see it, and if we are going to start now being concerned about how many people left and how many people stayed on, we are going to be sidetracked.

The main issue is, and I take it your client wants it adjudicated for future operations——

Mr. Mortenson: Not only my client but there are a lot of places looking at this. It is a very important issue.

(Testimony of James R. Westengard.)

The Court: ——is what is the situation when a night club offers this type of facilities and then does certain things at a certain hour to permit these people to become spectators and to partake, not whether or not they actually, as I see it, did some leave, did some see it, how many stayed, but the real issue is, here it was, you can have it. Now what is the situation?

Don't you agree with me on that?

Mr. Mortenson: Yes, but unfortunately he has a regulation to deal with. We keep running into these problems all the time. Out of a great generosity of the Commissioner's heart, he says, "I can impose a tax from breakfast until 2:00 a.m., but——"

Mr. McHale: It is the Congress, not the Commissioner.

Mr. Mortenson: This is the Commissioner's ruling that I am talking about. It is his interpretation of what Congress said.

But there is a generous concession that they will not impose this tax if a patron left before the show. That is why this is important, because if there is taxability at all you can't apply it under the regulations that the Government concedes to those who left.

The Court: Yes, you are quite right.

Mr. Mortenson: So it shouldn't be a problem, but it is.

The Court: You are quite right about that.

Mr. McHale: We submit, your Honor, first of all

(Testimony of James R. Westengard.)

there is an assessment which is prima facie evidence and has a presumption of correctness and that, as your Honor knows, the basis was the same as taxing the people in the other [158] room, the 94 persons who stayed to see the show and six who left. It is my basic opinion that Mr. Hover's testimony is not entitled to too much credence as to the proportion of people who stayed. He has certainly an interest in the suit, and the basis for his opinion is not very clear.

The Court: I would be inclined to agree with that.

Mr. McHale: So I think the real issue of Mr. Mortenson's case is this private party business. I don't see why we can't agree that this is typical.

The Court: I think it is something you ought to sit down together and work out and not do here in open court.

Mr. Mortenson: Very well.

The Court: If you can.

Mr. Mortenson: I would like to talk with Mr. McHale at the noon recess, and it is quite possible that we could save time of the court and time of the witnesses.

The Court: That may very well be. Do you think maybe we ought to recess now?

Mr. McHale: I have got these witnesses here, your Honor. I hate to hold them up. Each one takes a little time.

The Court: I know. What do you want to do?

(Testimony of James R. Westengard.)

If you are going to get a stipulation then they are excused.

Mr. Mortenson: Why don't we stipulate to everything except how many went home and just put them on for that purpose? We will stipulate to the rest. [159]

Mr. McHale: In other words, the stipulation will be with respect to the remaining witnesses except Mr. Stevens, whom I am calling for another purpose, that the testimony of the witnesses who preceded is typical and the others would testify except with respect to the number of those who stayed.

The Court: I think the best thing, gentlemen, is for you take the luncheon recess and work out something on paper. I really do, instead of doing it in this haphazard way, because apparently it is of some importance to you and it is of some importance to you, and you have offered a previous stipulation in writing and I think you ought to do it on this subject also, work it out in writing if you can.

Mr. Mortenson: Mr. McHale knows what the people are going to testify to. We can discuss it and perhaps reach a stipulation.

The Court: All right. But I also am concerned about a stipulation dealing with the balance of the 304 parties.

Mr. Mortenson: Here is the problem, every one of these 304 filed his tax with the District Director, who has an office in this building. I am under a

(Testimony of James R. Westengard.)

handicap. If their memory isn't too clear I know which way it is going to swing. So I practically have to depend on Mr. Hover's testimony. The Government has 304 and he has all the agents that he needs. They can interview all 304 if they want to. [160]

The Court: Can't we get a stipulation?

Mr. McHale: I don't think that is fair, your Honor.

The Court: Just a moment. Can't we get a stipulation with respect to all of these others with the exception as to what time the people left?

Mr. Mortenson: Yes.

The Court: All right. We have gotten that far.

In other words, the testimony of these nine or ten who would have been called is typical of the testimony which would have been elicited of the remaining number of private parties, with the exception of the time when the people actually left.

Mr. Mortenson: Yes.

Well, the curtain, probably we have to the opening of the curtain, but for those things we have no problem.

The Court: We have no problem but the problem.

I have tried to help you shorten your case during this Christmas season, but if you don't want to do it, go ahead. I am here to try it.

Mr. Mortenson: I want to get together with Mr. McHale.

The Court: I am going to recess for lunch at

(Testimony of James R. Westengard.)

this point and you talk it over, gentlemen. If you need your witnesses, you will simply have to keep them. I am sorry.

They are all instructed to return at 2:00 o'clock, but in the meantime I do want you and Mr. Mortenson to [161] discuss this.

The Witness: Your Honor, I have a boat this afternoon that I thought I would get on. Could I just finish my testimony?

The Court: Take his testimony.

Q. (By Mr. McHale): If I understand, you did not bring any papers of this party?

A. No, I have no records.

Mr. McHale: I offer this as the Government's exhibit next in order.

The Clerk: Defendant's Exhibit F marked for identification.

(The exhibit referred to was marked Defendant's Exhibit F for identification.)

Mr. McHale: I offer it.

The Clerk: Admitted.

(The exhibit referred to, marked Defendant's Exhibit F, was received in evidence.)

Q. (By Mr. McHale): This letter of December 5, 1952, is a letter agreement with Ciro's and was signed by you? A. That is correct.

Q. You have been sitting in the courtroom while these other witnesses have testified regarding the arrangements [162] for the Pavilion Room, have you not? A. Yes.

(Testimony of James R. Westengard.)

Q. Would your testimony with respect to the questions asked be the same? A. Yes.

Q. In every particular as the testimony of the other witnesses? A. Yes, I would say so.

The Court: How many people would you say remained to see the floor show here?

The Witness: Practically a hundred per cent.

The Court: How many people were in the party?

The Witness: Around 70, 75.

The Court: Did some of them go on the floor and dance?

The Witness: I don't think so.

The Court: All right. Any cross-examination?

Mr. Mortenson: No cross-examination.

The Court: You may step down.

(Witness excused.)

Mr. McHale: Does your Honor wish to recess now?

The Court: Will you have an internal revenue agent testify here?

Mr. McHale: I believe they will, your Honor.

The Court: Then I assume they will tell us how they made the selection of the people who have been subpoenaed? [163]

Mr. McHale: We can certainly do that.

The Court: So maybe we can draw some deduction as to whether or not this was a representative group.

Mr. McHale: I was going to have them testify as to statistics.

The Court: All right. We will recess until 2:00 o'clock.

(Whereupon, at 12:00 o'clock noon, a recess was taken until 2:00 o'clock p.m.) [164]

December 20, 1957, 2:00 P.M.

Mr. McHale: Mr. Clerk, I have a stipulation.

The Court: May I see it?

All right. File it.

The stipulation reads:

"It is hereby stipulated by and between the parties hereto, through their respective counsel of record, that if called and sworn as witnesses, a representative of each of the remaining 300 Pavillion Room parties (referred to in Plaintiff's Exhibit 2), and asked the same questions as the four witnesses who have previously testified, each would answer similarly to the answers of the four witnesses previously called regarding the Pavillion Room; it being understood, however, that a few organizations, exclusively male professional groups, not more than six in number, had regular business meetings during the period involved in the Pavillion Room, at which the accordion curtain was not opened and the floor show was not witnessed. This latter proviso is subject to further proof during the course of the trial."

Very well.

Mr. McHale: May that be admitted as an exhibit, your [165] Honor?

The Court: It is filed as a file paper. I don't

know what your practice is here. Do you want the stipulations as exhibits? They can be.

Mr. McHale: I don't know what the best practice is.

The Court: A stipulation can be made orally on the record, just as this is determined to be, but I think we will mark it as an exhibit.

Did we mark the other stipulation as an exhibit?

Mr. Mortenson: Yes, we did.

The Court: Then mark it as an exhibit.

The Clerk: That will be Exhibit G, Defendant's Exhibit G.

(The exhibit referred to was marked as Defendant's Exhibit G for identification.)

DEFENDANT'S EXHIBIT G

United States District Court for the Southern District of California, Central Division

No. 20853-WM Civil

HERBERT D. HOVER, dba CIRO'S,
Plaintiff,

vs.

UNITED STATES OF AMERICA,
Defendant.

STIPULATION RE THE CUMULATIVE EFFECT OF THE TESTIMONY OF PAVILLION ROOM WITNESSES

It Is Hereby Stipulated, by and between the parties hereto, through their respective counsel of

record, that if called and sworn as witnesses a representative of each of the remaining 300 Pavillion Room parties (referred to in plaintiff's Exhibit 2), and asked the same questions as the 4 witnesses who have previously testified, each would answer similarly to the answers of the 4 witnesses previously called regarding the Pavillion Room; it being understood, however, that a few organizations, exclusively male professional groups not more than 6 in number, had regular business meetings during the period involved in the Pavillion Room, at which the accordion curtain was not opened and the floor show was not witnessed. This latter proviso is subject to further proof during the course of the trial.

Dated: December 20th, 1957. [1]

/s/ ERNEST R. MORTENSON,
Attorney for Plaintiff.

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant United States Attorney, Chief, Tax Division;

/s/ EDWARD R. McHALE,
Attorneys for Defendant.

Received in evidence December 20, 1957 [2]

Mr. McHale: Then we will excuse as a witness Mr. Borisof.

I will call as a witness Mr. Marvin Stephens.

The Court: As I understand it, this written stipulation that was just filed as Exhibit G will take the place of the oral stipulation that we were attempting to formulate before the luncheon recess?

Mr. Mortenson: Yes, your Honor. [166]

MARVIN E. STEPHENS

called as a witness by and on behalf of the defendant, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name?

The Witness: Marvin E. Stephens.

Mr. McHale: I am sorry, your Honor; I was talking to that witness.

Your Honor understands that this is the stipulation that we were discussing?

The Court: Read back what I said, Mr. Reporter.

(The record was read by the reporter.)

Mr. McHale: That is correct, your Honor.

The Court: All right.

Direct Examination

By Mr. McHale:

Q. Mr. Stephens, what is your occupation?

A. I am a civil engineer for the Metropolitan Water District.

(Testimony of Marvin E. Stephens.)

Q. You arranged a party at the Pavillion Room during this period, didn't you? A. Yes, I did.

Q. For what group?

A. For the Employees Association of the Metropolitan [167] Water District.

Q. Do you have any letters, memoranda, of your arrangements for that party?

A. Yes, I do.

Q. Will you produce them, please?

I ask the clerk to mark as defendant's next in order Ciro's file of the Metropolitan Water District Employees Association, party in Pavillion Room for Friday, May 14, 1954.

The Clerk: Defendant's Exhibit H, marked for identification.

(The exhibit referred to was marked as Defendant's Exhibit H for identification.)

Mr. McHale: I offer it in evidence, your Honor.

The Court: Admitted.

Mr. Mortenson: No objection.

The Clerk: Admitted.

(The exhibit referred to was received in evidence and marked as Defendant's Exhibit H.)

Q. (By Mr. McHale): Would you examine Exhibit H, please? You will find in there a white letter dated March 22, 1954, addressed to you, and at the bottom marked "Approved and accepted, Marvin E. Stephens." Is that your signature?

(Testimony of Marvin E. Stephens.)

A. That is.

Q. That is the letter agreement for the party at Ciro's, is that correct? [168]

A. That is the confirmation, yes.

Q. Prior to this date, Mr. Stephens, did you have other correspondence with Ciro's regarding this party?

A. Yes, I did, in a letter of inquiry pertaining to holding a party at Ciro's.

Q. And you have brought that letter with you?

A. Yes.

Q. The reply, is that it? A. Yes.

Q. That is a letter of January 6, 1954?

Mr. Mortenson: One moment, please.

Mr. McHale, when we entered into this stipulation, you told me there was going to be another witness, and that witness would testify to matters other than those covered by the stipulation, is that correct?

Mr. McHale: That's right. This is going to something different.

Mr. Mortenson: May I see that, please?

Mr. McHale: Let me have it marked for identification, please.

The Court: Make it H-1.

The Clerk: Defendant's Exhibit H-1 marked for identification.

(The exhibit referred to was marked as Defendant's Exhibit H-1 for identification.) [169]

Mr. McHale: I offer H-1 in evidence.

(Testimony of Marvin E. Stephens.)

The Court: It is admitted.

The Clerk: Defendant's Exhibit H-1 admitted in evidence.

(The exhibit referred to was received in evidence and marked as Defendant's Exhibit H-1.)

The Court: I take it there is no objection, Mr. Mortenson?

Mr. Mortenson: No objection.

Mr. McHale: That's all, Mr. Stephens.

The Court: Have you finished with him?

Mr. McHale: Yes, your Honor.

Your witness.

Cross-Examination

By Mr. Mortenson:

Q. Who signed that letter, Mr. Witness?

A. Dolores Miller, Mrs. Dolores Miller.

Q. Were your dealings with Mrs. Miller or Mr. Hover on this matter?

A. I dealt with Mrs. Miller.

Q. With Mrs. Miller, is that right?

A. That's right.

Q. Did you talk with Mr. Hover about this at all? A. No. [170]

Mr. Mortenson: That is all.

The Court: Is there going to be some questions here that Mrs. Miller——

Mr. McHale: I know there is one sentence that is

different there that they are going to make some point of.

The Court: You aren't going to raise any contention that Mrs. Miller wasn't authorized to speak for Ciro's?

Mr. Mortenson: No.

Mr. McHale: I didn't want to go into it any further on testimony. The only thing that is different in this letter——

The Court: Just a moment.

Yes?

Mr. McHale: The only thing different in this letter from the others, and the reason I have accepted this one, was that in this particular case mention is made that the increase in price is by reason of the federal tax.

The Court: Yes, I notice that.

Mr. McHale: Thank you, Mr. Stephens.

I forgot, your Honor. I am sorry. Mr. Woodmansee, this takes care of you, too, our stipulation.

That concludes the witnesses I had on the Pavillion Room group, your Honor. We can resume with Mr. Hover on cross at this time.

The Court: Mr. Hover, take the stand. [171]

HERBERT D. HOVER

recalled as a witness, having been heretofore duly sworn, was examined and testified further as follows:

Cross-Examination
(Resumed)

By Mr. McHale:

Q. Mr. Hover, I believe you testified with respect to your talent, your arrangement for talent in the main room. First of all, you testified that you were open on a seven-day week, 365 day a year basis; is that correct?

A. Well, most of the time we were on a seven-day week, yes, sir.

Q. You weren't dark any time?

A. We may have been dark, but basically we were on a seven-day week.

Q. When you contracted for talent, that is a floor show, floor show acts, you contracted so you would have acts in there all the time, didn't you? I mean you would always have someone playing?

A. Usually. Sometimes there was a period. But usually we did.

Q. Suppose you had a well-known act, such as one like people mentioned today, Les Paul and Mary Ford, suppose you had them on a two-week basis, what particular day would they start their run? Any particular day?

A. They would generally start the day after the closing [172] day of the previous attraction.

Q. But would there be any particular day of the week when you would ordinarily close or open?

(Testimony of Herbert D. Hover.)

A. I would say in the majority—I would say more attractions open on Friday night than any other night of the week, but we have had attractions open on every night of the week. But more of them open on a Friday night than any other nights—than any other night.

I hope I understand your question correctly.

Q. Yes. Then Friday night would be the night a new act would ordinarily open the majority of the times?

A. I don't know about a majority, but there were more on Friday than any other day.

Q. Supposing you were booking them on a two-week basis, would they play solidly seven days a week? A. Yes, they would .

Q. No days off in there? In other words, they would work every night for the period of the engagement?

A. Each contract was on its own, but in most cases they would work the two weeks.

Q. You would book your acts somewhat in advance, wouldn't you; you wouldn't wait until one act was in before you booked the next one?

A. We try to. Sometimes a few months, and sometimes we would book an act the same night it would open, if we were [173] in a difficult situation.

Q. But more commonly you would try to have it arranged in advance?

A. So far as we could, we would. But sometimes you can't do it.

Q. Suppose you had somebody, let's just for the

(Testimony of Herbert D. Hover.)

sake of argument or illustration say Les Paul and Mary Ford, going in on a Friday night for two weeks, and this is one of the ones you had booked in advance, suppose you had someone following them at the end of two weeks, when would the next one be booked in? On a Friday two weeks hence?

A. If we had an act—I am sorry to have interrupted you.

Q. That is all right.

A. If we had an act booked in opening on a Friday for a straight two weeks, that means the act would close on a Thursday, unless something else would happen, and in that case we would arrange for the following act to open on a Friday. Unless we may have had a closed house that Friday, or for some reason or other we wanted to open the act on Saturday. But there were different circumstances at all times in California, in L.A., which are different from situations existing throughout the country, where you book an act, let's say, for eight, 10, 12 or 14 weeks, but where we normally would book an act for two weeks we didn't have [174] too much to offer an act. We also paid less than they paid elsewhere, so we had to give in to acts in many instances.

Q. Let's take your illustration here of the act that starts on Friday and runs for two weeks. How would this 14—is that what you call it, 14 out of 15?—contract work? Is that what you call it?

A. Usually it would be like 14 out of 15 days,

(Testimony of Herbert D. Hover.)
if the act would agree to it. If they didn't agree to it, it would be straight 14 days.

Q. Suppose you had an act that would agree to 14 out of 15, would that mean that one night they wouldn't work?

A. No, it wouldn't mean that at all. It meant we had a right to lay the act off for a night. We had that right. It doesn't mean we did it.

Q. One night out of 14 or one night out of 15?

A. Well, if an act was signed for two weeks, but we had the right to play the act 14 out of 15 days, that means we had a right to lay the act off one day out of the 15. We had that right.

Q. You mean that you had a right to continue that act over until Saturday, instead of Friday?

A. No. We would have the right to play the act from a Friday, closing on a Friday, if we laid the act off one night.

Q. In other words, you would close Friday with the [175] act, you would start on a Friday and run through two weeks and then play that following Friday? A. If we did that.

Q. If you did that? A. Yes, sir.

Q. In other words, you would add onto their time. How much would you pay them? So much for their run, no matter whether they played 14 nights or 15 nights, or how would it work?

A. Well, if they worked 15 days out of 15, they would get what would correspond to two weeks' salary. But, you see, each case is different. For example, we had a case at one time where we had a

(Testimony of Herbert D. Hover.)

closed house, and we paid the act even though they didn't work. That happened many times, we would pay an act even though the act wouldn't work. Sometimes we would go to an act and ask for a concession, say, "Look, we have a chance for a closed house on Sunday, Sunday is an off night for you, doesn't mean anything to you, why don't you take Sunday off and we will close you on Thursday instead of Wednesday?"

Sometimes they would say yes, and other times they would say no.

Each case would depend on its own, depending on our relationship with the act, depending upon the future bookings of the act, how anxious the act was to get away from town, or [176] certain concessions we would make to an act. For an example, give them the privilege of playing a television play, or certain other concessions. Or whether the act was happy or not in the engagement. Many of them were temperamental and big-salaried people.

Q. What was your general way of paying them? Was it per night, per engagement, per week, per performance?

A. You pay an act so much per week, usually as we called it in those days, on a seven-day week. So that if they work a number of days you pay them pro rata, which means one-seventh of the week's pay, if they work extra days, or you might hire an act to work like 10 days for a certain stipulated amount, and if it included two week ends, you would pay them more than if it included one week end. In

(Testimony of Herbert D. Hover.)
other words, you take everything into consideration as well as you can and pay accordingly.

Q. Suppose you had an act that you are paying, let's say $2,000 per week—I don't know whether that is high or low—but let's say $2,000 a week.

A. To a night club owner it is high; to an actor, it is low.

Q. $5,000 a week, is that better?

The Court: No. That is worse for the night club owner. I think he would prefer $500.

Q. (By Mr. McHale): Let's say it was $5,000 a week, would [177] you pay that act one-fifth of that for every night they worked, is that the way it would work out? A. One-fifth?

Q. I mean one-seventh.

A. We pay them at the end of the week. If they open on a Wednesday, we pay them on Tuesday.

Q. Suppose they laid off one night, how much would you pay them—six-sevenths?

A. We would pay them a week on the eighth day. In other words, if an act opened on a Tuesday, the first week would normally be up on Monday when they would be paid. But if they were off one day, by a prearranged stipulation that they were not to be paid, we would pay them a week's pay on Tuesday night. So as they worked seven days out of eight, they would be paid on the eighth day rather than the seventh.

Q. Suppose that on Sunday night there had been a closed house in there, and they had worked for the closed house, they would just work seven

(Testimony of Herbert D. Hover.)

days and get paid, and suppose their pay for that night was the same as it normally would have been, would that have been seven days' work, then?

A. I don't think I quite understand that.

Q. Suppose we had a week situation, just a one-week booking. A. W-e-e-k?

Q. Yes, one week. And Sunday night there is a closed [178] house, but suppose that the organization has the regular act that is booked into Ciro's on that night, what is the normal thing, that they get paid six-sevenths of their normal week's pay and one-seventh from the group?

A. No, it doesn't work that way, sir.

Q. How does it work?

A. Well, let us say an act opens on a Wednesday night, the first week is up on Tuesday, normally, but they were off on Sunday, well that means that we get them for an opening night, for a Friday night, which is the best week night, and for Saturday night, so that act is more valuable to us on an opening night, Friday night, and Saturday night, than it would be on Sunday or Monday, so we would make certain concessions to an act. So that, as I said before, if we had an act, let's say for a 10-day period with two week-ends, we would have to pay that act more than if we had them for a 10-day period with one week-end. In other words, an act is not worth one-seventh of the weekly salary per day on any day; it is worth maybe three times more on a Saturday night to us, maybe three times more on an opening night, and maybe twice as much on a Friday night.

(Testimony of Herbert D. Hover.)

And on a Sunday night, sometimes we pay an act, if we had to pay an act, and even close down on a Sunday night, because it wasn't worth our while to bring in an orchestra and crew, and so forth, for the revenue we would take in. So it would depend on its own circumstances, [179] on the type of act, whether the act was, using the colloquial expression, hot at the time, what we had to pay the act and so forth.

Mr. McHale: That's all.

The Court: Do you have anything?

Mr. Mortenson: No redirect.

The Court: Step down.

Go ahead. Do you have anything further on your case, Mr. Mortenson?

Mr. Mortenson: The plaintiff rests, your Honor.

Mr. McHale: Mr. Harker.

GLEN H. HARKER

called as a witness by and on behalf of the defendant, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name?

The Witness: Glen H. Harker, H-a-r-k-e-r.

Direct Examination

By Mr. McHale:

Q. Mr. Harker, what is your business or occupation?

A. I am a representative of the General Electric Company.

(Testimony of Glen H. Harker.)

Q. Did you arrange for a party at Ciro's in 1954? [180]

A. I did.

Q. In the Ciroette Room on the second floor?

A. It was——

Q. Upstairs? A. Slightly up, yes.

Q. That was a group of all men, is that correct?

A. That is correct.

Q. How many in the party?

A. Approximately from 15 to 20.

Q. You had dinner? A. That's correct.

Q. And drinks or cocktails? A. Yes, sir.

Q. After the dinner was over did you go down into the main part of Ciro's? A. Yes, sir.

Q. And you saw the floor show?

A. Yes, sir.

Q. Where did you sit down there?

A. Well, to the right front, up front to the right of the stage.

Q. And you saw the complete floor show, your group did? A. Yes.

Mr. McHale: That is all. Your witness. [181]

Cross-Examination

By Mr. Mortenson:

Q. Do you recall, Mr. Harker, whether you had any drinks downstairs after you moved downstairs?

A. We did.

Q. Do you remember the price of the drinks?

A. No.

(Testimony of Glen H. Harker.)

Q. Do you recall whether it was more or less than what you had been charged upstairs?

A. I really don't know.

Mr. Mortenson: That is all.

The Court: Do you remember if every member of your party had a drink?

The Witness: I beg your pardon?

The Court: Do you remember whether every member of your 15 or 20 people who went down to see the show had a drink?

The Witness: I presume we did.

The Court: Before you had rented the Ciroette Room had you been told that you would be permitted to go down and see the show?

The Witness: I don't recall if we had made any such arrangements.

The Court: When you went down for show time did somebody from management take you down?

The Witness: I don't think so. [182]

The Court: You just wandered down by yourselves?

The Witness: I think so.

The Court: All right. Anything further?

Mr. Mortenson: No more questions.

The Court: Anything further?

Mr. McHale: No more, your Honor.

The Court: Step down, Mr. Harker.

Mr. McHale: The witness may be excused.

Mr. Schiever, please.

RAYMOND J. SCHIEVER

called as a witness by and on behalf of the defendant, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name, sir?

The Witness: Raymond J. Schiever.

Direct Examination

By Mr. McHale:

Q. What is your occupation, Mr. Schiever?

A. I am a claim approver for the Prudential Insurance Company.

Q. Did you arrange a party at Ciro's in 1951?

A. Yes, I did.

Q. In the Ciroette Room? [183]

A. Yes, sir, that's right.

Q. For what group?

A. For the employees of the claim division of the Prudential Insurance Company.

Q. Was it a mixed group, men and women?

A. Yes.

Q. With whom did you arrange the party, do you recall?

A. I believe the name was Miss Miller, the person I contacted.

Q. How did you do it? By telephone?

A. Yes, by phone.

Q. Was there any arrangement made whether or not you would see a floor show?

A. Yes, there was.

Q. What was the arrangement?

(Testimony of Raymond J. Schiever.)

A. Well, the arrangement was for a flat fee of a dollar fifty cents a person we would have the privilege of using the Ciroette Room and then would have the privilege of seeing the second floor show downstairs.

Q. At this particular party there was no dinner served, is that correct? A. No dinner.

Q. No dinner? A. No. [184]

The Court: What time did the party get started?

The Witness: Approximately 8:30.

Q. (By Mr. McHale): Did your group go down and see the second floor show?

A. Yes, they did.

Q. What was the floor show, do you recall?

A. If I can recall correctly, the headliner was a gentleman by the name of Daniels. It was similar to Billy Daniels, but it wasn't the same person.

Q. Was there a bar in the Ciroette Room?

A. Yes, there was.

Q. Did they have a bartender there?

A. Yes.

Q. Did your group go back up after seeing the floor show? A. Yes.

Q. Where did you sit, incidentally, when you were in the main floor to see the floor show?

A. It was in the rear, center in the rear, approximately in the neighborhood of their main bar downstairs.

Q. Was it raised up a little bit, the lounge?

A. Yes, it was raised a bit.

The Court: Was it a lounge, did you say?

(Testimony of Raymond J. Schiever.)

The Witness: If you would call it that. There was tables, just the same type tables as in the main floor. [185]

Mr. McHale: Your witness.

Mr. Mortenson: No cross-examination.

The Court: I want to ask you something. This $1.50 charge was just for the use of the Ciroette Room per person?

The Witness: Yes.

The Court: And you paid extra for every drink?

The Witness: Yes, we did.

The Court: What happened—your bill was tallied at the end of the evening?

The Witness: No. It was individually.

The Court: As each one took a drink, he paid for it?

The Witness: That's right.

The Court: What happened when you went down to the main room or the lounge? Did you have a drink there?

The Witness: Yes, sir, I believe we had.

The Court: And there you paid, also?

The Witness: Yes, for the individual drinks.

The Court: You may step down.

Mr. McHale: I have one more Ciroette Room witness, your Honor, but he is on call. He is about 10 minutes from the court house. Would this be an appropriate time to take a recess?

The Court: Have you got anything else you want to go ahead with in the meantime?

Mr. McHale: I haven't right at the moment. I

could call [186] Mr. Hover, of course, as an opposing witness under Rule 43(b), but I have another witness coming in at 3:00 o'clock.

The Court: Just a moment now.

Do you expect that other witness very shortly?

Mr. McHale: At 3:00 o'clock.

The Court: Not before 3:00 then?

Mr. McHale: No, I don't, your Honor.

The Court: All right.

Mr. McHale: I didn't realize that we would move along this fast this afternoon, after this morning.

The Court: All right.

(Recess taken.)

The Court: I want to get a few things straight on the record.

Do I understand that the show began at 10:30 at night?

Mr. Mortenson: Between 10:30 and 10:45.

The Court: All right.

And can we also agree that the accordion curtains were pushed back—what, a half hour before?

Mr. Mortenson: No. At 10:30.

The Court: At the time the show was about to commence, is that the idea?

Mr. Mortenson: Yes.

The Court: Do you also agree, gentlemen—I asked you this the first day, and I want to make sure that we understand [187] one another—that I will not have to sit down or hire Price-Waterhouse to do any accounting for me; that in the event I find that the parties in the Pavillion Room were private, let

us say, until the accordion curtains were pulled back, and public thereafter, that you gentlemen will agree between yourselves on the tax to be paid?

Mr. McHale: The answer is, your Honor, I think that Mr. Hover says he has the tapes from which we can compute the amount of sales at the time that the price went up, which was in most of the cases in the Pavillion Room.

The Court: Then the answer is yes?

Mr. Mortenson: Yes.

Mr. McHale: If we can find those tapes, we can make that computation. We can make that stipulation.

The Court: That will be a stipulation. So that in the event, when I write my opinion, if I do come to that conclusion, let us say, and as I say with all candor at this point I don't know what conclusion I am going to come to, I can say in there that the attorneys have agreed that with the resolution of the proposition of law in this fashion they will agree upon the amount of tax owing?

Mr. McHale: Your Honor understands as far as the government is concerned, we feel they have a burden here, a burden of proof, and that this would be merely an approximation under the so-called Cohan rule, the best we can do under the circumstances, [188] if your Honor came to that conclusion.

The Court: All right. That leads me to the next point.

I suppose this can be off the record.

(Discussion off the record.)

The Court: The dollar amounts I don't care about, you will agree between yourselves, and if I hold that way and a decree is finally submitted to me for signature, it will by agreement include the amount.

Mr. Mortenson: Yes. We now have stipulated that when we get the tapes, Mr. McHale and I, in accordance with our present oral stipulation will stipulate to a dollar amount of tax.

The Court: In the event that the decision is that it was private before 10:30 and public after?

Mr. Mortenson: Yes. I presume it would read that the sales were so much, and 20 per cent applied to that would be so much, if you found that the 20 per cent applied.

The Court: You are getting me into the very thing I don't want to get into. I want you gentlemen to agree or not agree that if I hold it is a public performance after 10:30 you will then agree upon the amount of tax that is owing.

Mr. Mortenson: Very well. It can be done in that form, just as well as the other, yes.

The Court: Unless you have something better that you [189] would like to suggest. My mind is open.

Mr. McHale: Mr. Kroll.

HERMAN KROLL

called as a witness by and on behalf of the defendant, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name, sir?

The Witness: Herman Kroll.

Direct Examination

By Mr. McHale:

Q. What is your occupation, Mr. Kroll?

A. I work for the Los Angeles County Auditor's Office.

Q. And did you arrange a party at Ciro's for June of 1954? A. Yes.

Q. June 29th I believe the date was?

A. Yes, as I remember it.

Q. For what group?

A. It was a group of us from the accounting division in the auditor's office in honor of one of our employees who was retiring.

Q. Was it a mixed group? [190] A. Yes.

Q. About how many people attended?

A. Around 30.

Q. You made the arrangements yourself for his party? A. Yes.

Q. With whom?

A. With, I think it was, Dolores Miller.

Q. And——

A. And I contacted her by telephone, and I got a confirming letter.

Q. Do you have a copy of the letter of confirmation? A. Yes.

(Testimony of Herman Kroll.)

Q. You brought it with you? A. Yes.

The Court: Was that in the Ciroette Room?

The Witness: Yes, sir.

The Clerk: Defendant's Exhibit I marked for identification.

(The exhibit referred to was marked Defendant's Exhibit I for identification.)

Q. (By Mr. McHale): It was your understanding, as confirmed by this letter, was it not, that your group would be permitted to see the floor show at Ciro's? A. That's right.

Q. Did they have a bar in the Ciroette [191] Room? A. Yes.

Q. And a bartender up there? A. Yes.

Q. Did you have dinner? A. Yes.

Q. What time did your group arrive?

A. Around 7:00 o'clock.

Q. Then you were taken down to see the floor show, were you, downstairs?

A. No. As I remember it, we had dinner and drinks, and it was just a nice party, and it was the second floor show that we were invited as guests to witness.

Q. Do you remember what the attraction was that night? A. Eddie Albert.

Q. Where did you sit when you went down to see the floor show?

A. Right at the corner of the main room, just off of the stairs that go up to the Ciroette Room.

Q. You sat in the main room? A. Yes.

(Testimony of Herman Kroll.)

Q. Did you go back up afterwards?

A. Some did. I know some went up to get coats and hats. The party really broke up at that time.

Q. As soon as the show was over?

A. Yes. [192]

The Court: That was for the second show, did you say?

The Witness: Yes.

The Court: What time does that go on?

The Witness: By gosh, I don't remember. It was late.

Q. (By Mr. McHale): Would you say it was with relation to midnight, around midnight?

A. It was around that when we got out, as I remember it.

The Court: Well, that is the first show, isn't it? The first show goes on at 10:30. What time does the second show go on, Mr. Mortenson?

Mr. Mortenson: Usually a quarter of 1:00 or 1:00 o'clock.

The Witness: Well, it could have been that late. Gosh, I really don't remember. It has been a long time ago.

Mr. Mortenson: We might ask his wife, your Honor.

The Witness: If I didn't happen to have this letter, I would have forgotten the date.

The Court: It was one of those nights?

The Witness: It was a week day.

Q. (By Mr. McHale): Would you say it was a good party?

(Testimony of Herman Kroll.)

A. It was a very enjoyable party, yes, it was.

Q. What percentage of your group went down to see the show?

A. Well, as I remember, practically everybody. I didn't [193] check. Some probably stayed up and just kept drinking. I know I went down. I didn't check and herd them down. They were just asked to go down, and those who wished did. I know many did.

Mr. McHale: I offer the exhibit next in order. Your witness.

Mr. Mortenson: No questions.

The Court: Received.

The Clerk: Exhibit I received in evidence.

(The exhibit referred to was received in evidence and marked as Defendant's Exhibit I.)

Mr. McHale: Mrs. Miller.

DOLORES MILLER

called as a witness by and on behalf of the government, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name?

The Witness: Dolores Miller.

Direct Examination

By Mr. McHale:

Q. What is your present occupation, Mrs. Miller?

A. I am with the State Board of Medical Examiners.

(Testimony of Dolores Miller.)

Q. Did you at one time work for Mr. [194] Hover? A. Yes.

Q. What period of time?

A. From '47 to '56, June of '56.

Q. What were your duties?

A. Well, I went there as his secretary, and then I started taking over the banquet business, which was very small then, and built it up. I should say the last three or four years I was, I guess you could say banquet manager.

Q. We have noticed your signature on many of these agreements, and I assume that you were handling most of the arrangements for most of these banquets at Ciro's, is that correct? A. Yes.

Q. During the period involved? A. Yes.

Q. With respect to the Pavillion Room—Incidentally, what were your normal working hours?

A. Usually I arrived there about 9:15 or 9:30 and stayed as long as it was necessary.

Q. Were you around there in the evenings some of the time? A. Yes.

The Court: You mean 9:15 p.m., is that what you meant?

The Witness: A.M., sir.

Q. (By Mr. McHale): You were there some of the evenings? [195] A. Yes.

Q. Did you have occasion to observe, over the period of time that you were employed at Ciro's——

A. Yes.

Q. ——the practices with respect to the engagement of the Pavillion Room by these various ban-

(Testimony of Dolores Miller.)

quet groups? A. Yes.

Q. With respect to these parties that were booked into the Pavillion Room, was it the normal practice to advise them that they could see the floor show by pulling aside this accordion curtain?

A. Yes.

Q. And as a matter of fact was it the practice that most of these groups saw the floor show?

A. I should say most of them.

Q. There has been a stipulation presented in evidence here that there were a few groups that met rather regularly. A. Yes, sir, that's right.

Q. Perhaps once a month or perhaps not quite as often as that, but during all or part of the period involved, particularly groups of male professional men, groups like that? A. That's right.

Q. In the Ciroette and Pavillion Room I think these groups met. Do you recall any specific groups?

A. Well, the most regular one that I recall that was [196] in the Pavillion Room was a group of doctors. It was a medical fraternity.

Q. What was the name of the fraternity?

A. Phi Delta Epsilon.

Q. How often did they meet?

A. Once a month.

Q. How about the summer months?

A. Well, as I recall, most of the regular groups usually skipped August, I think, because so many were away on vacations and so forth. Some of them in July, too.

Q. This group would meet in the evening, I take

(Testimony of Dolores Miller.)

it? A. That's right.

Q. Would the sliding curtain be open for this particular group? Do you recall?

A. As I recall, in that particular group I should say that more often it wasn't open.

Q. It wasn't open?

A. No. Because, you see, being professional men, they had much to talk about among themselves, and then they did like to play bridge. I recall many occasions when they didn't care about seeing the show.

Q. Can you think of any other specific groups that met in the Pavillion Room to whom this applied on any kind of a regular basis?

A. Unless you consider a yearly party regular. We [197] had many groups who came back year after year because they liked it.

The Court: You mean once a year?

The Witness: Yes, sir.

The Court: Can you recall any yearly groups of this nature where they wouldn't care to see the show, that is what I am meaning when I am phrasing this question?

A. No, I don't recall any such group as that.

Q. This is the only one that you can recall?

A. Yes. I can't think of any other one that came in, as you say, regularly to the Pavillion Room. There may have been. Of course, I have been gone from there a year and a half.

Q. We are not concerned with the period since you have left there. Would you say that perhaps the situation was different in the Cirocette Room, which was a small room?

(Testimony of Dolores Miller.)

A. Yes. As I recall, we had about, I think—I know of two, and I think there were three groups that came in once a month over a long period of time.

Q. Would you say the size of the facilities had something to do with which room these groups that didn't care to see the show met in? I mean the size of the space available. Was that the reason they went in the Ciroette Room?

Mr. Mortenson: Just a minute, please. I object to that question, your Honor. I think that calls for what the parties [198] were thinking.

The Court: No, no. Let's find out whether that was discussed.

The Witness: I am afraid I didn't quite understand your question.

The Court: Well, let me ask you this: What caused either you or these people, if you know, to decide whether to rent the Pavillion Room or the Ciroette Room?

The Witness: I see. It was the number of people who were guaranteed to attend the party.

The Court: What minimum guarantee would you want for the Pavillion Room?

The Witness: As I recall, it was 75 persons.

The Court: Anything less, the Ciroette Room?

The Witness: Yes, sir.

Q. (By Mr. McHale): There is no regular group that you can recall of more than 75 people, that is, that would require the facilities of the Pavil-

(Testimony of Dolores Miller.)

lion Room, that would meet regularly, as opposed to once a year?

A. I am thinking now, when you say "regularly" of a certain period of time and regularly scheduled.

There were groups who came in oftener than other groups, perhaps three or four times a year, but I don't recall any offhand that came in more than once a month.

Q. Can you recall any of the ones that came in three, [199] four times a year?

A. I am sorry, I can't think of any specific name.

Q. Now, you dealt with most of the three hundred or so groups that I imagine scheduled the Pavillion Room during the period involved in this lawsuit, and you had conversations with most of the representatives of this group. Would you say that the opportunity to see the floor show was an inducement for them, offered to them as an inducement to book the Pavillion Room?

A. Well, I know that they liked it, of course, as anyone would.

Q. I mean, you sold that floor show, that was one of your selling points that booked the Pavillion Room, was it not?

A. I don't remember that I had to specifically hammer that point, because, you see, the Pavillion Room was a lovely room, and they liked it because it has its private entrance, and for many other reasons, and then many other private rooms in this town don't have private bars for the parties and

(Testimony of Dolores Miller.)

their own bartenders, and that sort of thing. I don't remember that I had to use that above anything else.

Q. With respect to the Ciroette Room, that was many times made an attraction of the room, that the group would be able to see the show?

A. No, I could never have promised them that, that [200] they could see the floor show from the Ciroette Room.

Q. Many times you said if the space were available, they could? A. If it were possible.

The Court: You said something about "above anything else," when you discussed the Pavillion Room as one of the selling features. Is it agreed that it was at least one of the selling features that they could see the show?

The Witness: Yes, I would say so.

May I add this? I do remember a few groups that cared nothing whatsoever about the floor show. They were interested more in the actual facilities of the room.

The Court: Well, I think we have a stipulation to that effect.

Q. (By Mr. McHale): Mrs. Miller, many of the agreements that you prepared and signed and sent out to Pavillion Room groups carried the notation that drinks would be 75 cents until show time and 90 cents thereafter? A. Yes.

Q. With whom did that originate, that particular phrase in the letter, or stipulation or contractual provision?

A. Well, as I remember, periodically we used to

(Testimony of Dolores Miller.)

have conferences to discuss the parties and the procedure regarding them, and so forth, and we would, may I say, hash things [201] over, and I don't remember any reason.

I think it just—of course, we must face the fact that we were having these parties to make money, make a profit, and I think it just seemed that if we could get 90 cents at that time we would get it.

Q. When you say "We would have conferences," who do you mean by "we"—you and who else?

A. Mr. Hover liked to call all of us together, the maitre d', sometimes even the bartenders if one were there in the late afternoon, if he would come in early he would attend, and myself, and anyone else who had anything to do with the parties and making them run smoothly, and so forth.

Q. By whose instruction was the price of the drinks set, that is, at 75 cents or 90 cents?

A. Fundamentally we must face the fact that Mr. Hover was the owner of Ciro's, and he had the last word on policies, but that price was set a long time ago. I don't really remember exactly why it was set. It was set because it seemed a good price, I think, and a fair profit.

Q. Would you read that letter, please, Defendant's Exhibit H-1?

Do you recall that?

A. Yes, I do, of course.

Q. Pardon? A. I do, of course. [202]

Q. You see the next to the last paragraph?

A. Yes, I notice here, "Drinks are 75 cents until

(Testimony of Dolores Miller.)

show time at 10:30. After that if you see the show drinks are 90 cents because we must add the entertainment tax."

So, evidently it did enter into it.

Q. That was a consideration then in the price?

A. Yes, it must have been.

Q. That is a letter that you prepared?

A. Yes.

The Court: Are you saying now that it went from 75 cents to 90 cents, the difference being represented to be the amount of the entertainment tax?

The Witness: In this letter I say so.

The Court: What caused you to say that? Was that pursuant to a discussion with Mr. Hover?

The Witness: I don't know.

You see, I wrote a great many of these on my own, and for some reason, probably because I had talked to this man—may I say this? That some groups wanted everything but very specifically. They were a little bit timid about coming to Ciro's, in the first place, because, as you know, Jack Benny was always making jokes about a cup of coffee costing a dollar and a half, and people were timid about coming there. So some of them wanted me to put everything in writing, make everything very, very clear, so that they [203] wouldn't have more costs thrown at them at the last moment or something.

The Court: The point that I want to get at is that you testified before that the drinks went from 75 cents to 90 cents simply because it represented a

(Testimony of Dolores Miller.)

good price and a fair profit, and you were there to make a fair profit; do you remember that?

The Witness: I didn't mean by that to imply that it couldn't have been that it was the entertainment tax. I just meant that I don't remember when we started charging that, if I had been told specifically at the time the difference was the entertainment tax. I do not remember being told that.

The Court: If you put it in that letter, would it indicate——

The Witness: This is to a specific group. They may have asked me to put that in, you see, in order that they wouldn't be charged that on top of the price that they had been quoted.

The Court: I understand. So that this statement to them was that that represented the entertainment tax?

The Witness: That's right, sir.

Q. (By Mr. McHale): Did you advise other groups of this over the course of the time involved?

A. I may have if they asked me. I mean—what I am trying to say, and perhaps I am not doing it very well, lots [204] of people when they take the responsibility of setting a party for a large group, they want to have everything in black and white, in order if further charges are added they won't be blamed for it.

Q. With respect to the closed house party, you also handled the arrangements? When I say "closed house," I mean when the entire facilities of Ciro's were reserved, that is, the main room, by one or-

(Testimony of Dolores Miller.)

ganization, for most of the evening, you handled those arrangements, also? A. Yes, sir.

Q. Were there occasions when a group would engage Ciro's for a night and use the regular entertainment that was booked into Ciro's during that run?

A. Yes, sir, there were several occasions of that sort. They would rather pay our entertainment and music to perform for them than to go to the trouble and expense of assembling what might have been a much less entertaining show.

Q. On some occasions you made the arrangements in advance as to who the checks would be paid to, that is, so much to the orchestra, so much to the entertainers? A. That's right.

Q. When you made arrangements like that, was that based on what those orchestras and those entertainers would have received that evening had it been a regular scheduled [205] event and Ciro's themselves been running it just open to the general public?

A. I don't remember. On some occasions they paid what they would get from us. I think on other occasions they paid—I think mostly they paid a little more, if I remember rightly. I always told them, you see, to call the orchestra leaders themselves, talk straight to them and make their arrangements with them, and I think sometimes they received more, perhaps, than they would have had we paid them.

Q. Weren't there several occasions, though, when

(Testimony of Dolores Miller.)

they said, "You handle it for us," and you handled it for them?

A. No. I always made it a point of stressing that. Because, for one thing, I didn't have time to do all of it, and I always wanted that to be strictly between them so that if anything went wrong I wouldn't be held responsible. Because that was their responsibility, actually.

Q. At the closed-house parties, so-called, where one group would reserve the main room for an evening, were there occasions when the engagement of the main room would be for part of the evening rather than the entire evening, that is, for the first show?

A. Yes, sir, I think we did have several parties like that where they would come in much earlier, of course, than our regular patrons would come in, and we would hold the room private for them until the middle of the evening, something [206] of that sort.

Q. Then the general public would be admitted after that?

A. Yes, if the group were small enough to allow that being done. So that there would be room in the main room for the public.

The Court: How often did that happen, do you know?

The Witness: Not too often.

The Court: We are dealing with 20 parties here, aren't we?

Mr. McHale: Yes.

(Testimony of Dolores Miller.)

The Court: We must have something specific on that, or a stipulation or something, Mr. McHale.

The Witness: I am sorry——

The Court: I was talking to counsel.

Mr. McHale: We have this, and the agent hasn't worked it out yet, if I may digress for a moment, we have examined the sales records of Ciro's for those 20 parties, and we find that I think on six occasions there are receipts that they consider taxable, as well as the so-called nontaxable receipts. We haven't gone over this with counsel, but I think we can arrive at a stipulation.

Mr. Mortenson: I think, your Honor, we can agree on that.

The Court: All right. [207]

Mr. McHale: I will attempt to have that ready Monday.

The Court: Were those other receipts attached?

Mr. McHale: Yes. In other words, part of them were. On those evenings there were taxable receipts and nontaxable.

The Court: So at least as to those six occasions your contention is going to be when they admitted the public it all became public?

Mr. McHale: All public.

The Court: As I understand, the parties took place in the main room on these occasions?

Mr. McHale: That's right, your Honor.

The Court: All right.

Q. (By Mr. McHale): Mrs. Miller, we have the folders of about 15 or 16 of these 20 parties that are

(Testimony of Dolores Miller.)

in issue in this suit. These are folders which I believe you kept. I am going to hand you the entire bunch and first ask you whether these are your folders on these parties. A. Yes.

Q. They are? A. Yes, sir.

Mr. McHale: I think perhaps, your Honor, we could mark them as parts of one exhibit, subdivide them.

The Court: Do they pertain to exhibits already in?

Mr. McHale: No. [208]

The Court: All right. Make it one, with subdivisions.

The Clerk: J and subdivisions. How many are there?

Mr. McHale: There seem to be nine.

The Clerk: That would be J-1 through J-9.

The Court: What are these now? Describe them for the record.

Mr. McHale: These, your Honor, are the Ciro's correspondence folders of the closed-house parties. These are of some of the parties that are in issue. All of these are in issue, but they are the only folders we have, I believe, or were able to locate.

Mr. Mortenson: May we have the former understanding that the doodles are not to be included, your Honor?

The Court: No doodles.

The Witness: I shall never doodle again.

Mr. McHale: May we take them in order, perhaps?

(Testimony of Dolores Miller.)

Q. Would you advise us for the record, please, what J-1 is, which party?

A. Are you speaking to me?

Q. Yes.

The Court: He is asking you to look at it and tell him what party it is.

The Witness: Zeta Beta Tau, Alpha Rho chapter.

Q. (By Mr. McHale): There is a letter in there dated March 13th—— [209]

The Court: What year?

Mr. McHale: 1952.

The Court: Go on. What is your question?

Q. (By Mr. McHale, continuing): ——to Mr. Goldring, in fact there are two letters, March 13th, there are two letters to Mr. Charles Goldring, and I am referring to the shorter letter. Would you look at that, please? A. Yes.

Q. In the second letter, the shorter letter, there is a sentence, "There will be one show at approximately 10:15. Should you decide to use other orchestras and acts than ours, we will be informed within a week from this date of March 13th." Can you determine from that letter whether this group was offered the regular Ciro's acts and orchestra?

A. It would sound so. Of course, this goes back to '52 when I answered you before about whether I had anything to do with the setting the price, or as a go-between between the acts and orchestras. In latter years I didn't. I had them talk between themselves. This goes back to '52, and at that time the party

(Testimony of Dolores Miller.)

volume wasn't as great, and I did attend to some of these, and this confirms an agreement that they would pay $500 to our acts and orchestras to appear for them.

Mr. Mortenson: May we have the record show what she is looking at now, please?

Mr. McHale: Yes. The witness is now looking at Exhibit [210] J-2.

Which is a letter to whom, Mrs. Miller?

The Witness: Mr. Jack Kotler.

Q. (By Mr. McHale): Which group, can you tell? A. Los Angeles Lodge No. 42.

Q. And it is dated February 22nd?

A. Yes, '52.

Q. You will note that there is a paragraph there which reads: "You have given me no guaranteed number of persons attending. At least one month before May 11th you will give us an approximate number. If this number has reached 300, Ciro's will be closed to the public on the night of May 11th."

A. That's right.

Q. Does that indicate that the question of whether or not this group was a closed party depended upon the number that would attend, is that correct? That is, whether or not the outside public——

A. That's right. That we wouldn't give them a closed house, in other words, for less than 300 persons.

Q. But nevertheless they would be booked into the restaurant, they would be given that number of

(Testimony of Dolores Miller.)

spaces, but other of the general public would be admitted, is that correct?

A. If they did not reach 300? [211]

Q. Yes. A. That's right.

The Court: We are dealing only with main room parties now?

Mr. McHale: That's right. What we designate for the sake of reference "closed-house parties."

Q. With respect to the closed-house parties, generally, Mrs. Miller, when a group reserved Ciro's for a night, such as one of these large groups taking over the main part of the restaurant, did Ciro's exercise any control over who could come to these parties?

Mr. Mortenson: That is objected to in form. I think she ought to be asked just what happened.

The Court: Overruled. Go ahead.

The Witness: Will you repeat the question, please?

The Court: Read it back, please.

(Question read by the reporter.)

The Witness: Do you mean by that how many could come?

Q. (By Mr. McHale): No. I mean who could come. Did you leave it in the hands of the group themselves, or Ciro's?

A. Of course it was their party, they could have whom they chose to have.

Q. It was entirely their responsibility?

A. That's right. [212]

(Testimony of Dolores Miller.)

The Court: And they simply guaranteed you a certain amount of money for a certain number of reservations, is that correct? For example, let us say that there were 200 places that they wanted in the main room, if 150 showed up they would still be responsible for 200, wouldn't they?

The Witness: Say if by the night before their party took place they had guaranteed 200, and only 150 showed up the next night, then we would have charged them the difference. Or if it were a charitable organization, we might have split the difference with them.

The Court: You mean you would give them up until 24 hours before to let you know, is that what you do?

The Witness: That's right.

The Court: If they don't advise you at all, then you assume it is for the number that they have reserved?

The Witness: That's right.

Q. (By Mr. McHale): The next folder I am going to show you, Mrs. Miller, is marked J-3, and there are letters in the file to a Mr. Nat Mallenstein, and they are both June 6, 1952, but the shorter letter in yellow contains a phrase, "At this time I cannot tell you what acts will be appearing here on that date, but if you will call me at a later date I shall hope to be able to tell you then."

Would that file indicate that Ciro's offered to this group the regular entertainment that would have

(Testimony of Dolores Miller.)

been booked [213] into Ciro's at the time that the party was scheduled?

A. Well, evidently—I do remember this group, and they were one that preferred to perhaps take a chance on the show that we were having in, because they believed that almost at any time we would have a better show than one that they could put together.

Q. The next folder that I am going to give the witness is marked J-4 and contains several letters.

A. Aren't they for two different years?

Q. Yes. Apparently they involve different occasions. Three letters are to a Mr. David S. Greenberg. Apparently one is an original and another is a copy to Mr. David S. Greenberg, and another letter of the same date, September 21, 1953, to Mr. David S. Greenberg, Midway Hospital. The shorter letter on yellow paper to Mr. Greenberg states:

"This will confirm our agreement that you will pay to Sammy Davis, Jr., the sum of $750 to appear for the party to be given on Tuesday, December 22nd, 1953, by the Midway Hospital, at Ciro's.

"I am sure, knowing Sammy, that he will be delighted to include some 'local' bits in his show.

"You will pay the sum of $225 for our large band and a rhumba trio. You will pay this sum [214] directly to the musicians."

Would this be another group which engaged the regular Ciro's acts and orchestra? A. Yes, sir.

Q. The next file I present the witness is marked J-5 and is addressed to what group, Mrs. Miller?

A. Save A Child Guild of Mount Sinai.

(Testimony of Dolores Miller.)

Q. And there is a short letter in the file dated February 17, 1953, to Mrs. Leon Esensten.

"Dear Mrs. Esensten:

"This will confirm our agreement that the Save A Child Guild of Mount Sinai will pay the sum of $375 for a show and two orchestras on the night of Sunday, November 8, 1953, for their party at Ciro's.

"This sum will be paid directly to the acts and to the musicians."

Would this be another party at which the group engaged the regular acts that would appear at Ciro's? A. Yes, sir.

Q. The next file is marked J-6. Will you state what group this is, Mrs. Miller?

A. Lions International Fourth District Convention.

Q. There is a short letter in the file, December 1, 1953, to Dr. Clyde Martyn. [215]

"Dear Dr. Martyn:

"This will confirm our agreement that the Lions International Fourth District Convention will pay the sum of $750 to our show and orchestras current on the date of their party to be held on Thursday, January 21, 1954, at Ciro's.

"The maitre d'hotel will inform you as to what part of this amount will be paid to the show and what part will be paid to the orchestras."

Would this be another such party where the group scheduled the regular Ciro's entertainment?

A. That's right.

(Testimony of Dolores Miller.)

Q. The next file is J-7. Will you tell us what group that is, Mrs. Miller?

A. Junior Helping Hand.

Q. And there is a letter in that file of June 11, 1954, to Mrs. Lee J. Goodman.

"Dear Mrs. Goodman:

"This will confirm our agreement that you will pay not less than $500 and not more than $600 to our show and orchestras current at Ciro's on the date of September 26, 1954.

"We shall advise you as soon as the show is booked for that period as to who will appear on the show and as to the exact amount you will pay to them [216] to appear for the Junior Helping Hand party to be given on September 26, 1954."

Is that another such party which utilized the regular acts booked at Ciro's? A. Yes.

Q. The next file is marked J-8. What group is this, Mrs. Miller? A. The Times Dealers.

Q. And there is a letter in there to Mr. Robinson dated January 18, and one paragraph reads:

"You will pay to our current show and orchestras not less than $500 and not more than $600. As the show at this moment has not been signed we cannot give you a more definite sum. However, as soon as the show is signed we shall notify you."

Would that indicate that that group was going to book the regular entertainment booked in Ciro's?

A. Yes, sir.

Q. The next file is J-9. Can you tell what group that is, Mrs. Miller? A. Culver City Hospital.

(Testimony of Dolores Miller.)

Q. And there is a letter in that file dated October 26, 1953, to Mr. William C. Hoppe, H-o-p-p-e: [217] "Dear Mr. Hoppe:

"This will confirm our agreement that the Culver City Hospital will pay the sum of $500 to our current show and orchestras on Thursday, December 17, 1953.

"Tentatively, we have arranged the schedule as follows: The rhumba band will begin playing at 8:00 alternating rhumba music with American music; the large American band will begin playing at 10:00.

"Your show will go on at approximately 10:00 or 10:30."

Would that be another such party where the regular entertainment was booked?

A. Yes.

The Court: Are you about through?

Mr. McHale: Your witness.

Mr. Mortenson: No cross-examination.

The Court: All right.

The Clerk: Your Honor, will these be admitted in evidence?

The Court: Yes, they are all admitted.

(The exhibits referred to were received in evidence and marked as Defendant's Exhibits J-1 to J-9.)

The Court: Recess until 10:00 o'clock Monday morning. [218]

Excuse me a moment. Before we recess, there is one other thing I want to get clear in my mind. I

think you raised the question of the statute of limitations for about four months. Can we take that out of the case here?

Mr. McHale: We filed a waiver, your Honor.

Mr. Mortenson: I didn't know they had waivers. It only involves $100, anyway.

The Court: Those are the issues that take the longest to decide.

All right. 10:00 o'clock.

(Whereupon, at 4:10 o'clock p.m. an adjournment was taken to 10:00 o'clock a.m., Monday, December 23, 1957.) [219]

December 23, 1957—10:00 A.M.

The Court: All right, gentlemen.

Mr. Mortenson: Ready for the plaintiff.

Mr. McHale: Ready for the United States. Mr. Penn take the stand please.

WARREN PENN

called as a witness by the defendant, being first sworn, was examined and testified as follows:

Mr. McHale: Before I commence with this witness, your Honor, earlier in the trial we told the court that we would have during the course of the trial stipulations as to what Ciro's books and records showed with respect to the receipt, or the recording of taxable receipts on the same night that closed house parties were scheduled, that is, the tax on the same night that closed house parties were scheduled, and the revenue agent has prepared such

(Testimony of Warren Penn.)

an exhibit showing that on six of the 20 taxed occasions there were some six receipts shown on Ciro's——

A. This deals only with six occasions?

Mr. McHale: It shows receipts on 20 parties and receipts on the six occasions as well as the 20 parties.

Mr. Mortenson: No objection.

The Court: All right, received.

(The document referred to was admitted in evidence as Defendant's Exhibit K.) [220]

Mr. McHale: I ask that at the close of the day's examination that the exhibit be withdrawn for photostating and returned. We can probably get it done today.

The Court: All right.

Direct Examination

By Mr. McHale:

Q. Mr. Penn, what is your occupation?

A. Well, I am retiring the first of the year as executive vice-president of National Electrical Contractors Association of Los Angeles.

Q. Well, you were with that association back in 1954, weren't you? A. Yes, sir.

Q. You arranged for a party at Ciro's restaurant? A. Yes, sir.

Q. With whom did you make the arrangements?

A. Well, the first party I talked with was a little girl named Miss Miller, I believe it was Dolores Miller, and then the night of the party the final ar-

(Testimony of Warren Penn.)

rangements were discussed with the maitre d' by the name of Johnnie; I don't know his last name.

Q. Mr. Oldrate?

A. I believe that was his name. It was a difficult name for me to remember.

Q. How far in advance do you recall you made these [221] arrangements of the party itself?

A. Well, we talked to Miss Miller quite a bit in advance because we were of the opinion that most of the places were sold out considerably in advance and I believe we talked to her oh, possibly two or three months in advance. Our request at that time was to try to get a date when there would be top-notch entertainment there.

Q. What sort of a party were you planning at Ciro's?

A. Well, a regular dinner party. We usually have about 250 or 285 people come and we give them the dinner free of cost, the association pays for it. They buy and pay for their own drinks, and then after that with their dinner we have just a couple or three short announcements, and we have the program come on.

Q. This was to be an occasion when you took over Ciro's restaurant, and not an occasion in which you took over just a room?

A. No, it was a closed night.

Q. What arrangements were made when you were planning this party with respect to entertainment, can you tell us?

A. Well, we made an arrangement whereby the

(Testimony of Warren Penn.)

—Cugat and his group would be there that night, and they were to be the entertainment on the program.

Q. Was Cugat and his group the ones that were currently playing at Ciro's at the time the party was there? [222]

A. That's what I understand, yes, sir.

Q. What arrangements did you make with Mr. Oldrate, the maitre d', with respect to payment for the entertainment?

A. Well, we understood that when we gave the dinner to our members free of cost to them that we could make an arrangement with the entertainment and pay them direct if we wanted to do that, and that is what we did.

Q. How did you pay for the entertainment, do you recall?

A. We made out a check direct to Mr. Cugat and a check was given to him.

Q. With whom did you discuss the amount of this check to Mr. Cugat?

A. With Mr.—what is his name?

Q. Oldrate. A. Yes.

Q. You never made any arrangements with Mr. Cugat with regard to this show?

A. No, I didn't talk to him.

Q. Or with any theatrical agents for Mr. Cugat?

A. No, none whatever.

Q. All your arrangements were made with the management, that is the personnel of Ciro's?

A. Yes, with Johnnie Oldrate.

(Testimony of Warren Penn.)

Q. To whom did you give the check made to Mr. Cugat? [223]

A. I had the check made out and Mr. Oldrate asked me if I had a check for the money, and I said: "Yes, I am going to give it to Mr. Cugat in a minute."

He said, "Give it to me and I will give it to him." So I gave him the check and I guess he gave it to them.

Q. Were there any people who were not members of your group admitted to the restaurant that night?

A. Yes, there was a very few.

Mr. McHale: Your witness.

Cross-Examination

By Mr. Mortenson:

Q. Mr. Penn, did you give more than one party at Ciro's?

A. Offhand I believe we gave three or four up there.

Q. On how many of those occasions were a few people let in from the public?

A. If I remember it this was the only one.

Q. What happened in that connection as far as you were concerned?

A. Well, I think Johnnie come to me and said, "Here are some friends of ours who we would like to have as guests to see the show," and they come and sat down at a table, about—I think it was six or eight of them, and Johnnie wanted to know if that would be all right with me, and I told him it would,

(Testimony of Warren Penn.)

providing if they had any food or drinks they would pay for it themselves and wouldn't put it on our bill, [224] and I think they stayed and saw the show; that was all.

Mr. Mortenson: No further questions.

The Court: When was this party had, do you remember?

The Witness: Yes, sir, I do; it was had on Friday, June 10, 1954.

The Court: May I see that last exhibit? I might say for the record that this is not one of the days that the Government asserts the outside public was admitted.

Mr. McHale: No, I think we didn't consider that this was of a substantial nature.

The Court: It is not included in the list as one for which any outside taxes were paid.

Mr. McHale: Thank you, Mr. Penn.

(Witness excused.)

Mr. McHale: Mr. Hirschhorn, please.

SOL HIRSCHHORN

called as a witness by the defendant, being first sworn, was examined and testified as follows:

Direct Examination

By Mr. McHale:

Q. Mr. Hirschhorn, what is your occupation?

A. At present I am executive director of the California Credit Merchants Association here in town.

(Testimony of Sol Hirschhorn.)

Q. Were you connected with that organization in early 1955? [225] A. I was.

Q. Did you arrange for a party at Ciro's restaurant? A. I did.

Q. With whom did you make the arrangements?

A. With Dolores Miller.

Q. Do you have any record of any papers or anything in connection with the making the arrangements?

A. I do. This is the contract (indicating).

Mr. McHale: Two letters dated November 1, 1954. I ask they be marked for identification.

The Clerk: Defendant's Exhibit L marked for identification.

Mr. McHale: I offer L as our next in order.

Mr. Mortenson: No objection.

The Court: Received.

(The document referred to was received in evidence as Defendant's Exhibit L.)

Q. (By Mr. McHale): When you made the arrangements for this party what type of a party was it to be, taking over of the entire restaurant?

A. Yes. This was a closed affair, it was our annual Merchandiser Award, where we make an award to the industry, to a manufacturer.

Q. At the time you made the arrangements for the party what arrangements did you make about entertainment at the [226] party?

A. We spoke about entertainment at the time and we told them that we would prefer entertainment.

(Testimony of Sol Hirschhorn.)

and when the question came it was specifically told to us that as far as Ciro's are concerned the contract was for food and for the food alone. I told them that I would like to have entertainment and if they could possibly get it for us. They told us at the time, rather, Miss Miller told us at the time she would be glad to help me, but it was specifically understood at the time that we could bring in our own entertainment and if possible, I told them to get their entertainment that was there that week, because we could get it at a lower cost than drawing in outside entertainment.

Q. What was the entertainment currently appearing at Ciro's the week of the party?

A. At the time of this contract there was no specific understanding as to any entertainment, because at that time they didn't know who would have booked for the night of the affair. Their bookings were usually about a month before. That night they had the Catherine Dunham show and Dick Stabile, that was the music, and they had a rhumba band, that was Jack D. Costanza.

Q. What arrangements were made for paying this entertainment?

A. We were to pay them directly as the contract, the [227] second contract that you have there provided that the entertainment was to be paid by us directly.

Q. How did you determine the amount they were to be paid?

(Testimony of Sol Hirschhorn.)

A. We set a budget of $600, that there would be no costs above that amount.

Q. How did you arrive at the amounts of the checks you wrote to the various entertainers?

A. Well, we were told how to divide the $600 the night of the affair.

Q. By whom?

A. It would be by either one or two persons; I have no independent recollection, either by this Miss Miller or this Johnnie, the maitre d', Johnnie——

Q. Oldrate. A. Oldrate, yes.

Q. You have brought with you, I assume, the cancelled checks. Is that correct?

A. I have them here. These are the three checks that represent the entertainment, and these two checks represent the food.

Mr. McHale: May these all be marked as sub-exhibits of our next exhibit in order?

The Clerk: Defendant's Exhibits M-1, M-2, M-3 are marked for identification. [228]

Mr. McHale: And as the next in order two sub-exhibits, the ones paying for the food, as N.

The Clerk: Defendant's Exhibits N-1, N-2.

Mr. McHale: At this time I offer Exhibits M-1, -2 and -3 in evidence.

Mr. Mortenson: No objection.

The Court: Received.

(The documents referred to were received in evidence as Defendant's Exhibits M-1, M-2 and M-3.)

(Testimony of Sol Hirschhorn.)

Mr. McHale: I offer Exhibits N-1 and N-2 in evidence.

Mr. Mortenson: No objection.

The Court: Received.

(The documents referred to were received in evidence as Defendant's Exhibits N-1 and N-2.)

Q. (By Mr. McHale): At this party you restricted the people attending in some way, did you?

A. Correct. Only to the invited persons or personnel from our organization.

Q. How many shows were provided, do you recall? A. One show.

Mr. McHale: Your witness.

Mr. Mortenson: No questions.

(Witness excused.)

Mr. McHale: Mr. David Greenberg. [229]

DAVID S. GREENBERG

called as a witness on behalf of the defendant, being first sworn, was examined and testified as follows:

Direct Examination

By Mr. McHale:

Q. Mr. Greenberg, what is your occupation?

A. I am a controller at the Midway Hospital.

Q. In 1953 were you connected with the hospital?

A. Yes, I was.

Q. Did you arrange for a party at Ciro's restaurant December 23rd, 1953? A. Yes.

(Testimony of David S. Greenberg.)

Q. What type of a party was this that was arranged, was it in any particular rooms of the restaurant? Will you explain?

A. Well, it was for the use of Ciro's that evening for the medical staff of the hospital.

Q. Who paid for the party?

A. The hospital paid for it as part of the dues of the medical staff.

Q. You are the one who made the arrangements for the party in advance? A. Yes.

Q. With whom did you discuss the party in advance, I mean, the arrangements? [230]

A. The arrangements were made with the lady by the name, I believe it was Miss Miller.

Q. Was that made some time in advance of the party?

A. Oh, about maybe a month to a month and a half.

Q. What arrangements did you make with respect to the provision of entertainment at the party?

A. That we were to have the regular show that evening.

Q. Did you know at that time what the regular show was?

A. I do not believe I knew at that time but we did know before the night of the party.

Q. What was the entertainment that was actually provided at the party? A. Sammy Davis, Jr.

Q. Was there other entertainment, orchestra and so forth?

A. Their regular orchestra, I believe was Dick

(Testimony of David S. Greenberg.)

Stabile, and a rhumba band, and I don't recall the name of the orchestra.

Q. How were the people admitted, by ticket, to the affair?

A. Each doctor was given two invitations and he was checked off at the door and the ticket, the invitations, were given to the waiters at the time the dinner was presented and we were to pay by the number of tickets presented. [231]

Q. How much space at Ciro's did you use, did you use the main room, I suppose the regular nightclub part? Did you use any other portion?

A. We used that main room and then as I recall there is a partition to the right as you enter, and that was opened, we used both those rooms.

Q. Do you have any papers of the arrangements you made with Ciro's?

A. All I have are the bills that were presented in 1952 and 1953.

Q. You mentioned bills for a party in 1952? These are the records of Ciro's restaurant party—the Midway Hospital had at Ciro's restaurant for the previous year? Is that correct? A. That is.

Q. They are contained in the files of the Midway Hospital of which you are controller?

A. That is correct.

Mr. McHale: I ask the bill of December 10, 1952, be marked for identification.

The Clerk: Defendant's Exhibit O.

(The document referred to was marked Defendant's Exhibit O for identification.)

(Testimony of David S. Greenberg.)

Q. (By Mr. McHale): You did not attend the December 10, 1952, party?

A. I was not connected with the hospital at that time. [232]

Mr. McHale: I offer as Government's next in order the records of the Midway Hospital with respect to the party held at Ciro's December 10, 1952.

Mr. Mortenson: If your Honor please, the party we are talking about here I believe refers to December 23rd, 1953; but I have no objection to these going in the record.

The Court: All right.

(The document referred to was received in evidence as Defendant's Exhibit O.)

Mr. McHale: I ask the clerk mark for identification a statement of Ciro's dated December 22, 1953.

The Clerk: Defendant's P is marked for identification.

Mr. McHale: I offer as next in order the statement of Ciro's Exhibit P for identification in evidence.

The Court: Does that deal with which party?

Mr. McHale: That is the party which Mr. Greenberg attended and arranged for.

The Court: Which one, December 22nd, 1953?

Mr. McHale: Yes. I am sorry. May I show it to the witness?

Q. You cannot at this time find the cancelled check with respect to this party? Is that right?

(Testimony of David S. Greenberg.)

A. I attempted to. We have had a revenue audit since that time so the checks were——

Mr. McHale: I offer to stipulate at this time that [233] the entertainment was paid by separate checks to Dick Stabile in the sum of $187; Tony Terran Orchestra, $99; Sammy Davis, Jr., $689, and Ciro's $3,511.10, plus $100 deposit made in September.

Mr. Mortenson: That would be less.

Mr. McHale: Less $100, yes. No, it was plus that, I think.

Mr. Mortenson: Well, the document will show that the total amount was $3,161.10, with a deposit subtracted of $100, leaving a total of $3,061.10, plus gratuities of $450, for a total of $3,511.10. So stipulated.

The Court: May I see it please?

Q. (By Mr. McHale): At the time you made the arrangements for the party did you know what show you wanted?

A. Not at the original preliminary checkup, no.

Q. What arrangements were made with Ciro's with respect to the entertainment?

A. Well, we just asked them for the regular show.

Q. What arrangements were made as to how you would pay them?

A. I don't recall any arrangements being made until after the evening was over, and that evening before we left we paid for the entertainment.

(Testimony of David S. Greenberg.)

Q. How did you arrive at the amounts, do you recall?

A. Well, it was a certain amount per dinner and then, if I recall, at that time we wanted a maximum figure, and [234] the dinner was to take care of a certain portion of that.

Q. How did you arrive at the amount the entertainers were to be paid, was that told to you by Ciro's?

A. That was told to us the evening of the affair, yes.

Q. Who was the entertainment, Sammy Davis, Jr.? A. Right.

Q. Do you recall whether people outside of the medical staff of the hospital attended this party?

A. There was nobody there while I was there.

Mr. McHale: Your witness.

Mr. Mortenson: No cross-examination.

Mr. McHale: Is there a Mr. Hoppe here?

(No response.)

Mr. McHale: That concludes the closed house witnesses, your Honor.

The Court: Very well.

Mr. Mortenson: We have a stipulation with respect to the closed house parties I think we can arrive at, and save some time on the witnesses.

Mr. McHale: I would stipulate and like counsel to stipulate that in arriving at the part of the assessment that relates to the closed house parties that the

agents examined the books and records of Ciro's and determined that during the period involved there were 32 occasions on which [235] apparently the entire facility, that is, the main room, had been reserved by one organization, and that using the criteria which the agents have used, that is, as to who furnished or provided the entertainment, that they eliminated from taxation 12 of those, and that the 20 parties which are the subject of this particular dispute are those in which they applied their criteria that the groups utilized the regular services and entertainment of Ciro's rather than providing their own entertainment.

Mr. Mortenson: I am agreeable to that stipulation but of course I am not stipulating that the criteria they used——

The Court: Is correct.

Mr. Mortenson: ——is correct.

The Court: No question about it.

Mr. McHale: Mr. Ross, will you take the stand?

The Court: You are not offering anything in connection with that stipulation, are you?

Mr. McHale: No, since we have stipulated, your Honor, I think it takes care of the ultimate facts, so why clutter the record?

CHESTER M. ROSS

called as a witness by the defendant, being first sworn, was examined and testified as follows:

The Clerk: State your full name, please. [236]

The Witness: Chester M. Ross.

Direct Examination

By Mr. McHale:

Q. What is your occupation, Mr. Ross?

A. I am internal revenue agent working in the Los Angeles area.

Q. How long have you been an internal revenue agent?

A. I have been in the Internal Revenue Service since October '49.

Q. What is your education and background?

A. I graduated from a local university, majored in economics and had quite a bit of accounting.

Q. Which university was that?

A. UCLA, University of California at Los Angeles.

Q. How long have you been working on cabaret tax or excise taxes?

A. I have been in the excise tax field audit group since, oh, July, 1952.

Q. During the course of your duties as internal revenue agent were you assigned examination of Herbert Hover, doing business as Ciro's restaurant?

A. I was.

Q. In connection with that you examined the books and records of Ciro's to determine whether

(Testimony of Chester M. Ross.)

they paid the [237] proper amount of tax according to the Government's standards? Is that correct?

A. Yes, sir, I did.

Q. Could you explain to the court how you arrived at the figure of 94 per cent of the receipts of the main room as being subject to the cabaret tax?

A. Well, in the examination of the taxable sales that the taxpayer had reported and compared with the total sales of the main room, disclose that 94 per cent of the main room receipts had been subjected to the cabaret tax. It was our feeling that on the basis or from the manner in which the Pavilion Room was operated that by and large those receipts, the Pavilion Room receipts should be taxed at approximately the same percentage.

Q. Mr. Ross, explain, will you, how the actual mechanics of charging or not charging the tax are handled in the main room and the lounge? I think that has been a point that has been a little unclear, and I thought perhaps you might clear that aspect of accounting.

A. By and large the patron seated in the main room and lounge, waiter checks are used and the total charges and the taxes are added to those checks as purchases are made, and the check is presented to the patron when he calls for it, or when he leaves. With respect to the lounge bar generally drinks are purchased and paid for as purchased [238] so that the taxpayer's practice has been to sub-total the lounge bar register at 9:00 o'clock, the purchases being run that register after 9:00 o'clock

(Testimony of Chester M. Ross.)

then are representing the taxable receipts. The difference in treatment generally arises from the fact that the bar purchases are paid for as purchased and there is no way of controlling who comes and who goes and whether the tax should apply or not except by the use of this method. We accept this method if we feel that the taxable receipts, or the cut-off hour reflected, if the cut-off hour receipts—subsequent to the cut-off hour—show a reasonable tax of the taxable receipts.

The Court: Is it your statement all bar purchases after 9:30 p.m. carry the tax?

The Witness: No, the checks themselves which are used for patrons that are seated, there is no difficulty as far as the management is concerned, if a patron leaves before the show there would be no tax added to that check.

The Court: Even if it is after 9:00 o'clock?

The Witness: Even if it is after 9:00 o'clock.

The Court: Supposing a new patron came in?

The Witness: If he actually stayed and didn't pay his check until he left, or remained after the show or dancing started by 9:30, then the tax would be added to the check.

The Court: So that at 9:30, is that when the tax begins? [239]

The Witness: I believe that is true, yes, sir.

Q. (By Mr. McHale): But the lounge bar purchases are paid for as purchased, so that the six per cent then represents the people who left before the entertainment, that is, the dancing started?

(Testimony of Chester M. Ross.)

A. The six per cent would represent the non-taxable portions; by and large, of that lounge bar tape, that is to say the ring-ups occurred before 9:00 o'clock and to some extent there may be some checks which were not taxed because patrons left before the dancing or entertainment, some few; there may also have been some checks to entertainers, which are not subject to the tax.

Mr. McHale: Your witness.

Mr. Mortenson: No cross-examination.

Mr. McHale: There is a waiver of the statute of limitations. I know in plaintiff's complaint, I think in paragraph 48, there was a contention made that part of these taxes may have been assessed too late. But there is a waiver.

Mr. Mortenson: Can't we simplify that by admitting that?

The Court: I thought I got that Friday.

Mr. McHale: Yes.

The Court: Off the record.

(Discussion off the record.)

Mr. McHale: The Government rests. [240]

Mr. Mortenson: There is just one further thing, your Honor. We are trying to locate these tapes. I wonder if I could have these marked for identification?

The Court: People's Exhibit 9.

(The exhibit referred to was marked Plaintiff's Exhibit 9 for identification.)

Mr. Mortenson: So that you might understand what it is we are trying to do, your Honor, I would like to——

The Court: Is that marked for identification?

Mr. Mortenson: Yes, just marked for identification.

The Court: Yes.

Mr. Mortenson: There is a date on each of these tapes and at a breaking point——

The Court: Where is the date? I don't see it.

Mr. Mortenson: In one case it is at the bottom, I believe, and the other at the top.

The Court: This is the Pavilion Room, June 21st, 1953?

Mr. Mortenson: Yes. At one point you will note that "75" stops recurring and "90" starts in, and then at the end of the tape it jumps from key No. 1, there is a Roman one to the right, over 2, 3 and 4.

The Court: Yes.

Mr. Mortenson: And then with Ciro's, that is the way of closing out a tape to show that the evening is over.

The Court: I see. [241]

Mr. Mortenson: So that when we find a tape we can determine how much the sales were after the prices were increased.

I don't know what we are going to do if we don't find the tapes, but I am going out this afternoon and see if I can help. The bookkeeper Mr. Hover had during this period is no longer there.

The Court: Once again, I want to get this part of it clear. Mr. McHale, I want you to listen to me.

Mr. McHale: Yes, your Honor.

The Court: Whether you locate the tapes or don't locate the tapes, as I understand it you gentlemen will stipulate as to the amount of tax owing in the event that I enunciate the principle of law that is applicable.

Mr. Mortenson: I don't know just how we are going to go about this. You are going to be in this afternoon, Mr. McHale? Then I will discuss this with you so that we can arrive at a method before we reconvene, so that there can't be any dispute as to how we are going to do this; if we have the tapes there is no problem.

The Court: Off the record.

(Discussion off the record.)

Mr. McHale: If your Honor announces a decision in which the amount of tax depends on the record, and so forth, I am sure we can stipulate as to the amount. It's a [242] mechanical problem and I am sure we can agree upon that.

The Court: That is the point I am trying to get at. Now, gentlemen, what is your wish? You are finished with your presentation of evidence, is that correct?

Mr. Mortenson: Yes.

The Court: Both sides rest. You will have your final briefs for me Thursday morning?

Mr. Mortenson: Yes, your Honor.

Mr. McHale: Yes, your Honor.

The Court: Do you want to make a brief argument Thursday?

Mr. Mortenson: Yes.

The Court: What do you want to adjourn to, the usual time of 10:00 o'clock?

Mr. Mortenson: Yes, I would prefer it to 10:00 o'clock.

The Court: All right, court is adjourned to 10:00 o'clock Thursday morning.

(Whereupon, at 10:50 o'clock a.m. the hearing was adjourned to reconvene at 10:00 o'clock a.m., December 26, 1957.) [243]

Thursday, December 26, 1957, 10 A.M.

The Clerk: Case No. 20853-WM Civil, Hover vs. United States of America, for further trial.

The Court: All right, Mr. Mortenson.

Mr. Mortenson: If the court please, before we proceed with the arguments, I believe we have a stipulation to be entered.

Mr. McHale: Well, I want to say something about that, your Honor, as your Honor has requested in the event that your Honor reaches a decision on one party's theory of the case that we could agree. Now, I said that I thought we would be able to, and Mr. Mortenson and I have sat down and gone over what we could agree upon and we have come to this agreement which we have made in writing, which is essentially this: We could agree upon probably when the drinks were served and when the meals were served, and we do that completely on estimates, but the plaintiff doesn't have any records, or just fragmentary records. I think

the ones that were introduced for identification were the only ones we have been able to find, of the time at which payments were made.

So the only agreement we can come to is when the service of food was made and I think we can pretty clearly agree that it was made before show-time and before the hour of [246] 10:30 p.m., and as to when the drinks were served we just sat down and figured the approximate time upon the refreshments served and prorated that before 10:30 and after 10:30.

The Court: What is your agreement on that?

Mr. McHale: It is reduced here to the dollar amounts for the Pavillion Room, as to what the tax would be if it were computed on that basis. Of course, the Government doesn't agree that this is a proper basis. So we believe that if your Honor's decision should be upon this basis, then it could become a part of the case.

The Court: Well, it should be filed. It is worded in the alternative, isn't it?

Mr. Mortenson: Yes, it is.

Mr. McHale: I want to make the specific objection.

The Court: Let me ask you this: What do you refer to in your stipulation, Mr. Mortenson? It is stipulated "That two-thirds of the refreshments were served to the patrons of the Pavillion Room before show time of 10:30 p.m. and one-third thereafter." Is that the substance of your agreement?

Mr. Mortenson: That is the substance.

Mr. McHale: The actual substance. As you re-

member, Plaintiff's Exhibit No. 1 showed that it was $55,581.98, taxes assessed on Pavillion Room receipts and on this theory, that is as to when drinks and refreshments were served or taken to the parties in the Pavillion Room, the $39,980.08 would [247] represent the tax on the food served and $10,401.27 would represent the taxes on beverages served prior to 10:30 p.m., leaving $5,200.63 representing the taxes on the beverages served after 10:30 p.m. Of course, the Government doesn't believe this is the proper criteria.

The Court: I understand.

Mr. McHale: But this is what we can agree upon, subject to our objections as to materiality and relevancy.

The Court: All right. It will be filed.

Mr. McHale: And further I want to state, of course, that this is just an approximation and goes to the whole Government theory on the burden of proof here, that the plaintiff didn't have records.

Mr. Mortenson: I might say, your Honor, on that, we gave an awful lot on that.

The Court: There is no sense of arguing that point now. The point is that that is a stipulation and you are agreeing to it in the event I may decide it based on that theory of law.

Mr. McHale: Based on the time of service.

The Court: The approximation is not strictly correct. That is an agreement, an understanding, as I understand it?

Mr. McHale: We want to make it clear we cannot stipulate that that is the time the payments

were made, as to either the meals or the beverages, because we submit it just cannot [248] be determined.

The Court: All right.

Mr. McHale: The evidence is conflicting.

Mr. Mortenson: If Mr. McHale is going to make anything of that argument, I would like a few minutes of rebuttal on that issue, because I don't think it has been briefed.

The Court: Proceed with your argument.

Mr. Mortenson: May I have a few minutes for rebuttal argument when Mr. McHale is through?

The Court: I will see. If it is necessary.

Mr. Mortenson: Thank you.

(Argument on behalf of plaintiff, by Mr. Mortenson.)

(Argument on behalf of Defendant, by Mr. McHale.)

(Closing argument on behalf of Plaintiff, by Mr. Mortenson.)

The Court: I will reserve decision. [249]

Reporters' Certificate

We hereby certify that we are duly appointed, qualified and acting official court reporters of the United States District Court for the Southern District of California.

We further certify that the foregoing is a true and correct transcript of the proceedings had in

the above-entitled cause on the dates specified therein, and that said transcript is a true and correct transcription of our stenographic notes.

Dated at Los Angeles, California, April 17, A.D. 1958.

/s/ J. D. AMBROSE,

/s/ AGNAR WAHLBERG,

/s/ SAMUEL GOLDSTEIN,

/s/ THOMAS B. GOODWILL.

[Endorsed]: Filed July 18, 1958.

[Title of District Court and Cause.]

CERTIFICATE BY CLERK

I, John A. Childress, Clerk of the above-entitled Court, hereby certify that the items listed below constitute the transcript of record on appeal to the United States Court of Appeals for the Ninth Circuit, in the above-entitled matter:

A. The foregoing pages numbered 1 to 198, inclusive, containing the original:

Complaint.

Answer.

Order for Pretrial Proceedings.

Amended Answer and Counterclaim.

Notice to take Deposition upon oral examination.

Defendant's Law Memorandum.

Reply to Counterclaim.

Defendant's Pretrial Opening Statement.

Plaintiff's Memorandum of Law.

Plaintiff's Supplemental Memorandum of Law.

Government's Analysis of Stipulation of Joint Exhibit 2-B.

Stipulation re Computation.

Plaintiff's Second Supplemental Memorandum of Law.

Minute Order 12/19/57.

Minute Order 12/20/57.

Minute Order 12/23/57.

Minute Order 12/26/57.

Opinion.

Motion for New Trial.

(Copy.) Proposed Findings of Fact, Conclusions of Law and Judgment, lodged 2/14/58.

(Copy.) Memorandum for Computation of Judgment.

Objections to proposed Findings of Fact and Conclusions of Law.

Defendant's Reply to the objections to proposed Findings of Fact and Conclusions of Law.

Affidavit of Service by Mail re Defendant's reply to the objections to proposed Findings of Fact, etc.

Motion for New Trial and Motion to Amend and make Additional Findings of Fact and Conclusions of Law.

Plaintiff's Memorandum in opposition to Motion for New Trial and Motion to Amend and make Additional Findings of Fact and Conclusions of Law.

Findings of Fact, Conclusions of Law and Judgment.

Order Denying Motions for New Trial and Motion to Amend and make Additional Findings of Fact and Conclusions of Law.

Affidavit of Service by Mail re motion for extension of time to docket cause on appeal and order.

Notice of Appeal.

Motion for extension of time to docket causes on appeal and order, filed 6/5/58.

Designation of Contents of Record on Appeal.

Motion for extension of time to docket causes on appeal and order thereon, filed 7/11/58.

(Copy.) Letter dated 3/13/58 from Judge Kaufman re denial of motion for new trial.

B. Plaintiff's Exhibits—1, 2, 3-A, 3-B, 3-C, 3-D, 4-A, 4-B, 4-C, 5, 6, 6-A, 7, 8 and 9.

Defendant's Exhibits—A, B, C, D, E, F, G, H, H-1, I, J-1, J-2, J-3, J-4, J-5, J-6, J-7, J-8, J-9, K, L, M-1, M-2, M-3, N-1, N-2, O and P.

C. Reporter's Transcript of Proceedings had on: 12/19/57, 12/20/57, 12/23/57 and 12/26/57.

I further certify that my fee for preparing the foregoing record, amounting to $2.40, has not been paid by appellant.

Dated: July 14, 1958.

[Seal] JOHN A. CHILDRESS,
Clerk;

By /s/ WM. A. WHITE,
Deputy Clerk.

[Endorsed]: No. 16106. United States Court of Appeals for the Ninth Circuit. United States of America, Appellant, vs. Herbert D. Hover, Doing Business as Ciro's, Appellee. Transcript of Record. Appeal from the United States District Court for the Southern District of California, Central Division.

Filed: July 21, 1958.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals for the Ninth Circuit

No. 16106

UNITED STATES OF AMERICA,

Appellant,

vs.

HERBERT D. HOVER, dba CIRO'S,

Appellee.

STIPULATION RE USE OF ORIGINAL EXHIBITS

It Is Hereby Stipulated by and between the parties hereto, through their respective counsel of record, as follows:

1. That the exhibits admitted into evidence in The Trial Court are voluminous in number and include several schedules large in size and newspaper clippings difficult to reproduce.

2. That the expense of reproducing the exhibits in the printed record would be considerable, and difficult of attainment in a form easily legible.

3. That it is agreeable to the parties that the exhibts be considered by the Court in the original form and referred to in the briefs of the parties.

4. That this stipulation is without prejudice to either party designating one or more of the exhibits for printing in the appellate rocord.

5. That all of the exhibits introduced into evidence in the Trial Court, that is, Exhibits 1 through 7, inclusive, and A through P, inclusive, are material to the consideration of the appeal and may be considered by the Court in original form and need not be printed.

Dated: July 22, 1958.

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant U. S. Attorney
Chief, Tax Division;

/s/ EDWARD R. McHALE,
Attorneys for Appellant.

/s/ ERNEST R. MORTENSON,
Attorney for Appellee.

[Endorsed]: Filed July 24, 1958.

[Title of Court of Appeals and Cause.]

CONCISE STATEMENT OF POINTS UPON WHICH APPELLANT INTENDS TO RELY

[Rule 17.6]

Comes Now the appellant, the United States of America, pursuant to Rule 17.6 of this Court, and states that it intends to rely upon the following points in its appeal of the above-entitled case:

1. The District Court erred in failing to award judgment for the defendant on its counterclaim in the full amount prayed for, $81,819.07, together with interest according to law.

2. The District Court erred in concluding that the statute imposing the cabaret tax was not intended to cover all the amounts paid for admission, refreshments, service or merchandise by or for those patrons of Ciro's who were entitled to be present during any portion of the public performance and in concluding that the tax was limited only to those amounts paid for refreshments, service and merchandise served during the time of the performance. (Concls. Law Para. I, IV.)

3. The District Court erred in concluding that the words, "entitled to be present" in the applicable statute did not apply to the Pavillion Room or Ciroette Room parties. (Concls. Law Para. 11.)

4. The Court erred in concluding, with respect to the Pavillion Room operation, that the amount of tax applicable to the drinks served after 10:30 p.m. is a proper measure of the tax. (Concls. Law Para. IV.) Appellant submits that the evidence is undisputed that the appellee failed to maintain records required by law showing the amounts paid by or for the patrons entitled to be present and has failed to sustain his burden of proof of showing the assessment was erroneous. Because of that, the entire amount of the tax assessed against the Pa-

villion Room was proper and should have been adjudged due and owing the United States.

5. The District Court erred in concluding that the tax assessment on five per cent of the Ciroette Room's receipts was improper. (Concls. Law Para. V.)

6. The District Court erred in concluding, with respect to the "Closed House Parties," that the payments received by Ciro's did not entitle the patrons or guests to be present during public performances for profit. (Concls. Law Para. VII.)

7. The District Court erred in concluding that upon the occasions in which the public was admitted to the "Closed House parties," that the receipts of the "Closed House parties" were not subject to the cabaret tax. (Concls. Law VI.)

8. The District Court erred in failing to conclude that plaintiff's failure to make and keep adequate records (Finding III, R. 103), of the amounts paid by or for those patrons or guests of the Pavillion Room for food, refreshment or merchandise who witnessed the entertainment, was in dereliction of Treas. Reg. 43 § 101.32(b), (1)-(4) inclusive, and thus, was fatal to his bearing his burden of proving the Commissioner's assessment of the tax on the Pavillion Room was erroneous.

9. The District Court erred in denying each of the defendant's motions for new trial, for each and every one of the grounds set forth therein, which are herein incorporated by reference.

10. The District Court erred in denying the defendant's Motion to Amend and Make Additional Findings of Fact and Conclusions of Law, for each and every one of the grounds set forth therein, which are herein incorporated by reference.

11. The evidence was insufficient to justify the following determinations of the District Court set forth in its Opinion and said determinations are clearly erroneous:

(a) Upon conclusion of the floor show, most of the guests at the private parties of the Pavillion Room left the building.

(b) The patrons by or for whom the charges in the Pavillion and Ciroette Rooms were incurred were seemingly members of private parties.

(c) The 304 parties in dispute with respect to the Pavillion Room were private up to 10:30 p.m.

(d) The operation of these so-called private parties is not so intimately related to the general operation of the Main Room, and the viewing by the Pavillion Room guests of the entertainment at 10:30 p.m. such an integral part of their evenings activities, that it can be reasonably inferred that the compelling motive in reserving the use of the Pavillion Room was for the purpose of seeing Ciro's entertainment.

(e) The private groups availing themselves of the facilities of the Pavillion Room did not consider themselves as part of the public patronage of

Ciro's and any intent on their part of being assimilated into the general over-all cabaret atmosphere of Ciro's was of incidental significance in their decision to conduct their parties in the Pavillion Room.

(f) The receipts prior to the removal of the separation in the Pavillion Room and the commencement of the floor show are outside the scope of the cabaret tax and were improperly included within the assessment.

(g) That $5,200.63 represents the correct tax assessment on the Pavillion Room operation.

(h) The amount of drinks served after 10:30 p.m. rather than the payments received for food, refreshment and merchandise, whenever sold, represent the correct measure of cabaret tax liability.

(i) The tax assessment on 5% of the Ciroette Room receipts is improper.

(j) With respect to the Closed House parties, the entertainment was furnished by the private groups rather than by Ciro's.

(k) That Ciro's did not furnish the entertainment on the 20 evenings in issue.

(l) That on 6 of the 20 nights in question the private groups had concluded their parties and surrendered the premises before the general public was admitted.

12. The District Court erred in determining that the United States is entitled to any less than the

full amount of tax assessed with respect to the Pavillion Room, because plaintiff failed to make and keep adequate and sufficient records of the amounts paid by or for patrons or guests of the Pavillion Room for refreshment, service and merchandise, who witnessed the public performance for profit and, consequently, failed to overcome the presumption of the validity of the Government's assessment of the tax.

13. In its Opinion, the District Court erred in construing the statute imposing the cabaret tax, and, most particularly, in not concluding that all of the amounts paid by or for the patrons or guests of the Pavillion Room entitled them to be present at a public performance for profit and thus, were subject to the tax. (Opinion—R.105-114, 116-117.)

14. The District Court erred in failing to find and conclude that the desire to be present at the cabaret performance was the major consideration for the groups in question to engage the facilities of Ciro's cabaret, whether they were: the Main Room, the Pavillion Room, the Ciroette Room, or the entire facilities of the cabaret for the so-called "Closed House parties."

15. The District Court erred in failing to conclude that the failure of plaintiff to come within the exception of § 101.14(c) of Treas. Reg. 43 is dispositive of the entire issue raised by the tax upon the Pavillion Room receipts.

16. The District Court erred in failing to adopt the following findings proposed by the defendant which are supported by the substantial weight of the evidence (commencing at R. 130): XIII; XIV; XV; XVI; XX; XXI; XXII; XXIV; XXV; XXIX; XXXI; XXXIII; that portion of XXXVII beginning with the second sentence through the end; XXXVIII; XXXIX, and the last sentence of paragraph XL.

17. The District Court erred in making its Findings of Fact XIX, XX, XXXI, and XXXII in that said findings are contrary to the evidence and are clearly erroneous.

Dated: July 25, 1958.

LAUGHLIN E. WATERS,
United States Attorney;

EDWARD R. McHALE,
Assistant U. S. Attorney,
Chief, Tax Division;

/s/ EDWARD R. McHALE,
Attorneys for Appellant.

Affidavit of Service by Mail attached.

[Endorsed]: Filed July 26, 1958.

No. [illegible]

[illegible]

[illegible] Circuit Court of Appeals

[illegible] FOR THE NINTH CIRCUIT

[illegible] V. [illegible],

Appellant,

vs.

[illegible] Hotel Policy Business as Corp.,

Appellee.

[illegible] Appeal From the Judgment of the United States District Court for the Southern District of California.

BRIEF FOR THE APPELLANT

[illegible]

[illegible]

[illegible]

[illegible]

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[illegible]

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FILED

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No. 16,106

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant,

vs.

HERBERT D. HOVER, Doing Business as Ciro's,

Appellee.

On Appeal From the Judgment of the United States District Court for the Southern District of California.

BRIEF FOR THE APPELLANT.

Opinion Below.

The opinion of the District Court [R. 44-63] is reported at 158 F. Supp. 179.

Jurisdiction.

This appeal involves a deficiency in cabaret taxes assessed[1] against the taxpayer by the District Director of Internal Revenue on or about November 14, 1955, for the period June 1, 1951, to March 31, 1955, in the amount

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[1]The complaint alleges [R. 12] that part of this assessment was barred by the statute of limitations but it was admitted at the trial that a waiver of such statute had been filed. [R. 327, 346.] Thus all of the assessment was timely.

of $67,660.62. [R. 112.] On or about August 2, 1956, the taxpayer paid $300 of such assessment and filed a timely claim for refund of such amount on that date. [R. 15-16.] Subsequently on September 20, 1956, an amended claim for refund of the same amount was also filed. [R. 19-20.] This claim was rejected by the District Director by a letter dated December 5, 1956, and sent by registered mail. [R. 21.] Within the time provided in Section 3772 of the Internal Revenue Code of 1939 and Section 6532 of the Internal Revenue Code of 1954 and on December 21, 1956, a suit for refund was instituted by a complaint filed in the District Court. [R. 3-21.] Jurisdiction was conferred on the District Court by 28 U. S. C., Section 1346. On September 4, 1957, the United States, appellant herein, filed an amended answer and counterclaim for collection of the balance of the cabaret taxes above referred to and interest in the sum of $81,819.07 together with interest from July 1, 1957, until paid. [R. 22-30.] A reply to the counterclaim was filed by the taxpayer on September 10, 1957. [R. 30-31.] On February 28, 1958, the District Court entered judgment (1) decreeing that the taxpayer take nothing by his complaint for refund of $300, and (2) that United States have judgment against the taxpayer on its counterclaim in the amount of $7,463.86 together with interest thereon until paid. [R. 125.] The motion for new trial and the motion to amend and make additional findings of fact and conclusions of law which were filed on behalf of the United States were denied by an order filed March 31, 1958. [R. 127-128.] Notice of appeal from the above judgment and order was filed on May 14, 1958. [R. 128-129.] This Court has jurisdiction under 28 U. S. C., Section 1291.

Questions Presented.

1. Whether the District Court erred in holding that the statute imposing the cabaret tax was not intended to apply to all amounts paid for the designated items during an evening at a cabaret by patrons who have attended private parties but who are entitled to be present and are present at the cabaret's public performance, and also in limiting the tax to amounts paid by such patrons during the cabaret's public performance.

2. The District Court held that taxability of preperformance payments by patrons of private parties should depend upon the motive of the patrons in coming to the cabaret. Assuming *arguendo* that this statutory interpretation is correct, the question is whether the District Court erred in concluding that the floor show was not a cogent reason for the selection of Ciro's cabaret by such patrons but was merely incidental to other reasons.

3. Whether the District Court erred in not entering judgment for the full amount of the taxes assessed (less the $300 paid by the taxpayer) inasmuch as the taxpayer failed to overcome the presumption of correctness attaching to the assessment by the production of proper records or by other proof.

4. Whether the District Court erred in finding that under the evidence here the entertainment for the patrons of the "Closed House" parties was furnished by such patrons rather than by Ciro's, and for that reason the cabaret tax cannot be imposed on payments made by such patrons.

Statutes and Other Authorities Involved.

The pertinent provisions of the statute and other authorities appear in the Appendix, *infra*.

Statement.

The facts as found by the District Court are as follows [R. 112-122]:

On November 14, 1955, cabaret taxes in the amount of $67,660.62 and interest in the amount of $7,858.51 were assessed against Herbert D. Hover, d/b/a Ciro's, for the period June 1, 1951, through March 31, 1955. Upon notice and demand for payment being made, Mr. Hover (referred to herein as taxpayer) paid $300 leaving an outstanding balance of $75,219.13. [R. 112-113.][2]

The above assessment represented additional taxes assessed with respect to three phases of taxpayer's operation for the period involved, namely, the Ciroette Room, the Pavillion Room and the "Closed House" parties. The amount assessed was determined by Revenue Agents who examined the taxpayer's books and records and who applied the cabaret tax to a certain percentage of the receipts of each room on a basis more fully explained below. The taxpayer, not having considered the receipts here in issue as taxable, did not segregate any portion of such receipts as cabaret taxes in his books and records. Also taxpayer kept no records showing what, if any, proportion of the persons who attended the parties in the Pavillion Room stayed for the floor show or for dancing. [R. 113-114.]

Ciro's is a famous night club located on Sunset Boulevard in Los Angeles. It is subdivided into three rooms in which the services and facilities of the club are offered to the public. These are the main entertainment and

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[2]Taxpayer has conceded that $992 of the taxes assessed was attributable to its "Main Room operations" and was owing because of a clerical error and is not in issue. [R. 113.]

dining room (referred to here as the "Main Room"), the Pavillion Room and the Ciroette Room. Ciro's has widely advertised its entertainment and in its advertisement has also offered the facilities of the Pavillion and Ciroette Rooms for banquet groups. One of the several inducements for such gatherings in those rooms was the opportunity to view the floor show. [R. 114, 116.]

Pavillion Room.

The Pavillion Room is located adjacent to the lounge and is separated therefrom by a movable wall and thick, soundproof curtain. The lounge is a slightly elevated portion of the Main Room and the Pavillion Room is further raised, thereby creating a six-step elevation differential between the Pavillion Room and the Main Room. Because of this added height the patrons sitting in the Pavillion Room can view the entertainment in the Main Room when the separation wall and curtain are withdrawn by looking through the adjacent lounge. Since the stage is located at the other end of the Main Room, obtaining a good perspective of the floor show from all portions of the Pavillion Room is difficult in view of the distance involved, and those in the rear of the Pavillion Room must move their seats into the fore part of that room in order to view the show. [R. 114, 117.]

Though ingress and egress to both rooms is possible by way of the lounge, the Pavillion Room also has its own separate entrance. Rest Rooms are shared in common with the Main Room, though entrance can be made from the Pavillion Room itself. Each room has its separate dance floor and band stand. Tables and chairs used in the respective rooms seem to be of a different character and their arrangement dissimilar. The building plans further disclose that the two rooms were not con-

structed as one unit but that the Pavillion Room was added long after the Main Room had been in existence. Upon the closing of the partition separating the two rooms there is an atmosphere in the Pavillion Room of complete privacy. [R. 117-118.]

The Government assessed a cabaret tax on 94 per cent of the receipts attributed to 304 private parties conducted in the Pavillion Room. The 6 per cent of the receipts excluded from the tax represents amounts paid for food, refreshment or merchandise by patrons who are presumed to have left prior to seeing the floor show. While there is some variation in the way these 304 parties were conducted, usually private organizations would contact Ciro's to arrange for the exclusive use of this room on a particular night. A contract would be negotiated and a deposit secured. Generally the service of the dinner would commence around 7:00 p.m. and terminate before 10:30 p.m. and was completed before the floor show began. During that time the movable partition separating the Main Room from the Pavillion Room would remain closed and the parties would have complete privacy. Depending on the nature of the organization, speeches, awards, community singing, local entertainment or dancing to music either piped in from the Main Room or furnished by their own hired orchestra might follow the dinner. In any event at approximately 10:30 p.m. the separation was usually removed so as to enable the groups to view the floor show in the Main Room. [R. 114-115, 118.]

The patrons attending the dinner in the Pavillion Room expected to be able to see the entertainment in the Main Room, as it was the understanding, whether committed to writing or not, that the so-called private parties would be afforded this privilege. Upon conclusion of the floor

show, most of the guests at the private parties left the premises. In view of the removal of the partition at or about 10:30 p.m., there was a public performance in regard to the Pavillion Room guests from that time on but the 304 parties in dispute were private up to 10:30 p.m. [R. 115-116.]

The District Court stated that the floor plan and structural layout of the Main Room and the Pavillion Room compels the finding that two separate and distinct rooms were contemplated by Mr. Hover and that it was intended that Ciro's would acquire the private party business by offering the privacy necessary to these organizations in the execution of their customry meetings or gatherings while affording them the opportunity of functioning in a well-known establishment like Ciro's. The District Court also stated that a comparison of the respective operations of both rooms further discloses an intent on the part of the management to treat the rooms other than as a single unit. There are some 25 basic differences in the operations of the two rooms. These include differences in menus, prices, services, working hours and duties of the waiters, manner of payment, parking fees, and cover charges. [R. 116-118.]

Any intent by the private organizations of being assimilated into the general over-all cabaret atmosphere of Ciro's was of incidental significance in their decision to conduct their parties in the Pavillion Room. These groups did not consider themselves as part of the public patronage at Ciro's. Their conscious choice to reserve the Pavillion Room indicates that the prime moving consideration in selecting that room was the desire to achieve some sense of privacy for their group activity and business—at least until the entertainment began. [R. 118-119.]

Upon the removal of the partition at show time, the Pavillion Room guests did observe and participate in the public performance in common with the other patrons in the Main Room and no distinction between the two rooms is warranted during that period. The position of the Pavillion Room guests during this period is analogous to the patrons of the lounge during the show or to the late-comers to the Main Room, who because of the crowded conditions existent there, are forced to stand at the bar in the lounge in order to see the floor show. Any payments from drinks or refreshments made by these patrons were, of course, subject to the tax. With respect to the $55,581.98 assessed against the Pavillion Room receipts, the parties have stipulated that $5,200.63 would represent the tax on food, refreshment or merchandise served to patrons or guests subsequent to 10:30 p.m. No admission charge was made to enter the Main Room from either the Ciroette Room or the Pavillion Room. [R. 119-120.]

Ciroette Room.

The Ciroette Room like the Pavillion Room was used primarily to accommodate private gatherings. However, unlike the Pavillion Room, it was located on the second floor of the building and those patrons desiring to see the floor show could do so only by descending a flight of stairs and passing through two doorways to the Main Room. The taxpayer permitted members of private organizations using the Ciroette Room to see the entertainment at 10:30 p.m. Some 5 per cent of the Ciroette patrons did in fact avail themselves of this opportunity. The Government assessed a cabaret tax based on 5 per cent of the receipts taken in by the Ciroette Room. It was stipulated that if any tax is due it is to be computed

on the basis of 5 per cent of these receipts and the only question presented for consideration is whether as a matter of law the cabaret tax applies to this 5 per cent. [R. 120.]

As the nature of the private parties in the Ciroette Room was similar to those conducted in the Pavillion Room, the above findings on this subject were held to be pertinent here and were incorporated by reference. [R. 121.]

Closed House Parties.

Part of the initial deficiency assessment consists of a tax on all amounts paid for admission, refreshment, service or merchandise on twenty evenings when all the facilities of Ciro's were reserved for the members of one particular organization and these are referred to as "Closed House" parties. On such occasions, the show and orchestras usually provided were the same as was regularly staged by Ciro's and Ciro's advised the private organizations as to the amount and distribution of the payments to be made to the performers if the private organizations should hire them. The private organizations themselves contracted for the entertainment and music supplied to the "Closed House" parties. In all cases checks in payment were made payable by the private groups to the performers. Private groups could, if they so desired, rent the Main Room without the Ciro entertainment and could furnish instead their own entertainment and orchestra. When the Ciro entertainers were retained by the private groups they were able to exercise control over the time when the performers would commence and the type of performance. Any service rendered by Ciro's was purely advisory and for the convenience of the private group. [R. 121-122.]

The District Court found that Ciro's did not furnish the entertainment on these twenty evenings in issue. The private organizations remained free to reject the regular entertainment appearing at Ciro's and if they chose to engage such performers, could modify their acts to suit their own purposes. Although on 6 of the 20 nights in question the public was admitted, the public was admitted only after the private groups had concluded their private parties and surrendered the premises. [R. 122.]

From the above findings, the District Court reached the following conclusions of law [R. 122-124]:

I. The statute imposing the cabaret tax is not intended to cover those pre-performance parties by those patrons whose desire to be present at the public performance was incidental to some more cogent reason for attending the carbaret, such as a private gathering of a private group or organization for the conduct of its business.

II. The words "entitled to be present" in the statute do not apply to the Pavillion Room or Ciroette Room parties where the main purpose of the parties engaging such rooms was other than to be present at the entertainment.

III. If the parties had ended before the commencement of the floor show or if the partition had remained closed and the Pavillion Room patrons excluded from entering the Main Room or observing the entertainment therein, the expenditures before 10:30 p.m. would not lie within the scope of the tax, even if the group using the Pavillion Room had arranged for their own entertainment, since under the statute there would be no public performance.

IV. It has been stipulated that the $5,200.63 representing the tax on drinks served after 10:30 p.m. is equivalent to the tax on the amounts paid for food, refreshment and merchandise by or for patrons or guests of the Pavillion Room entitled to be present during such performance for profit and is the correct amount of tax on the Pavillion Room operation. The court concluded that the sum of $5,200.63, is the proper tax on amounts paid by or for patrons in that room for food, refreshment or merchandise after 10:30 p.m.

V. The tax assessment on 5 per cent of the Ciorette Room's receipts is improper.

VI. After the private groups had concluded their parties and surrendered the premises, the club subsequently reverted to a cabaret status and this has no bearing on the nature of the parties from which the public was rigidly excluded.

VII. With respect to the "Closed House" parties, the payments received by Ciro's did not entitle the patrons or guests to be present during public performances for profit.

VIII. The Government is entitled to judgment on its counterclaim for the tax on the amounts paid for refreshment in the Pavillion Room after 10:30 p.m. and for its costs.

The District Court then entered judgment denying the taxpayer's claim for refund of the $300 which he had paid on the additional assessment and allowed the Government $7,463.86 (with interest) on its counterclaim. [R. 125.]

Statement of Points to Be Urged.

1. The District Court erred in failing to award judgment for the Government on its counterclaim in the full amount prayed for, $81,819.07, together with interest according to law.

2. The District Court erred in concluding that the statute imposing the cabaret tax was not intended to cover all the amounts paid for admission, refreshments, service or merchandise by or for those patrons of Ciro's who were entitled to be present during any portion of the public performance and in concluding that the tax was limited to those amounts paid for refreshments, service and merchandise served during the time of the performance.

3. The District Court erred in concluding that the words, "entitled to be present" in the applicable statute did not apply to the Pavillion Room or Ciroette Room parties.

4. The District Court erred in holding with respect to the Pavillion Room operation that the amount of tax applicable to the drinks served therein after 10:30 p.m. (when the floor show began) is a proper measure of the tax due on account of amounts paid by or for patrons in that room who were entitled to be present at the show.

5. The District Court erred in not holding that the taxpayer had failed to keep records required by law as to the amounts paid for food, refreshment or merchandise by or for patrons of the Pavillion Room who were entitled to and did witness the show in the Main Room, and in not holding that the taxpayer had failed to sustain his burden of showing that the assessment was erroneous.

6. The District Court erred in concluding that the tax assessment on five per cent of the Ciroette Room's receipts was improper.

7. The District Court erred in concluding, with respect to the "Closed House" parties, that the payments received by Ciro's did not entitle the patrons or guests to be present during public performances for profit.

8. The evidence was insufficient to justify the District Court in finding (1) that the operation of the parties in the Pavillion Room was not so intimately related to the general operation of the Main Room and that viewing of the show at 10:30 p.m. in the Main Room was not considered such an integral part of the activities of parties in the Pavillion Room, that it can be reasonably inferred that the compelling motive in reserving the Pavillion Room was to see Ciro's entertainment, and (2) that Ciro's did not furnish the entertainment for the twenty Closed House parties involved here.

9. The District Court erred in determining that the United States is entitled to any less than the full amount of tax assessed with respect to the Pavillion Room because the taxpayer failed to keep adequate records as to payments made by patrons who witnessed the public performance and failed to overcome the presumption of the validity of the Government's assessment of the tax.

10. The District Court erred in failing to find and conclude that the desire to be present at the cabaret performance was a major consideration for the groups in question to engage Ciro's facilities whether they were the Pavillion Room, the Ciroette Room, or the entire facilities for the so-called "Closed House" parties.

Summary of Argument.

1. This appeal involves a cabaret tax assessment on amounts paid by or for patrons of the so-called "Closed House" parties at Ciro's and also on those amounts paid by or for patrons at private parties in Ciro's Pavillion and Ciroette Rooms. The latter amounts were paid for items served before Ciro's floor show began. It is conceded that Ciro's is a cabaret, that its floor show and music for dancing constitute a public performance within the meaning of the applicable statutory provision, and that the payments made by persons who are patrons of its Main Room and lounge and who are entitled to be present at its floor show are subject to the cabaret tax.

Specifically the statute imposes this tax on all amounts paid for admission, refreshment, service or merchandise at a cabaret by or for any patron or guest who is entitled to be present during any portion of the public performance given by the cabaret for profit. The language used in such statutory provision is clear and simple and should be interpreted so that it will be given its commonly understood meaning. In applying this provision, it has been the policy of the Government to tax all amounts paid by or for patrons and guests at private parties given in the cabaret providing such patrons are entitled to be present and are present at the cabaret's public entertainment. We submit that this is a fair and proper application of the statute.

However the District Court held that the statute cannot be given its literal meaning, and emphasized particularly that the statutory words "all amounts" and "entitled to be present" cannot be applied to the preperformance payments by or for patrons at private parties in the Pavillion and Ciroette Rooms at Ciro's unless it be shown that

the desire to see the floor show was a compelling reason for such patrons' attendance at Ciro's. We submit that this makes taxability of such payments depend upon a subjective test and that there is no authority in the statute for such a test, and if applied would make administration of this statutory provision very difficult, if not impossible. Moreover, the District Court was not warranted in relying on *La Jolla Casa De Manana v. Riddell,* 106 F. Supp. 132 (S. D. Cal.), affirmed *per curiam,* 206 F. 2d 925 (C. A. 9th), because that case is not only distinguishable on its facts but the Government's interpretation of the statute here is in accord with the decision reached therein.

2. However assuming *arguendo* that the District Court's interpretation of the applicable statutory provision should be followed, we submit that its decision should still be reversed because its conclusion is contrary to the evidence and some of its own findings of fact. The evidence shows that the patrons composing the private parties at Ciro's were very much concerned with the opportunity to see the floor show and that they not only expected to see it when they came to these parties but Ciro's also held out its show and other public entertainment as an inducement for such parties both in its widespread advertisement and in the personal contacts made with the representatives of the groups giving the parties. Such evidence clearly indicates that Ciro's floor show was a cogent reason for the parties.

3. A presumption of correctness applies to the tax assessment here and the taxpayer had the burden of overcoming such presumption by producing evidence. However although the law requires the taxpayer to keep adequate records covering his daily operations and receipts

he admits that no record was kept of the number of patrons at private parties in the Pavillion Room who remained to see the show in the Main Room after the curtain between the two rooms was drawn back. The taxpayer has also failed to produce any other evidence to show that the basis on which the tax was imposed on receipts from patrons of the Pavillion Room was in any way incorrect. Therefore under either interpretation of the statute referred to herein, the District Court should have entered judgment for the United States in the full amount of the taxes and interest asserted.

4. During the period involved twenty "Closed House" parties were held by private organizations at Ciro's. These parties were not only held at the usual hours when Ciro's was customarily open and operating but they had the same shows and orchestras which were being used by Ciro's at the time the parties occurred. Also employees of Ciro's actually made the arrangements for such entertainment. It is the position of the Government that the arrangements made by these private organizations with Ciro's should be regarded merely as a reservation of tables. We also submit that although such groups were required to make separate checks for the entertainment, Ciro's actually furnished the entertainment. Thus the District Court was in error in not imposing the cabaret tax on payments by these groups.

ARGUMENT.

I.

The District Court Erred in Holding That the Statute Imposing the Cabaret Tax Was Not Intended to Cover All Amounts Paid for the Designated Items by or for Patrons Entitled to Be Present During Any Portion of a Cabaret's Public Performance, and in Concluding That the Statute Limited Such Tax to Amounts Paid for Refreshments Served During the Time of the Performance.

A. Introductory.

No question has been or can be raised as to the classification of Ciro's restaurant as a cabaret within the meaning of the applicable statute. It is also admitted that Ciro's has usually presented a floor show in its Main Room about 10:30 p.m. which constituted a public performance under the statute. The taxpayer (as owner of Ciro's) has regularly reported and paid a cabaret tax on the amounts received from patrons in its Main Room and adjoining lounge. During the period here this tax was limited by the taxpayer to 94 per cent of such receipts, it being presumed that 6 per cent was paid by patrons who did not remain for the entertainment. The Government accepted that estimate and in assessing the taxes involved here on receipts from patrons of the Pavillion Room, used the same percentage in computing the tax due on such amounts. [R. 46-47, 344-346.] But the District Court disallowed most of this assessment as it limited the tax on receipts from patrons in the Pavillion Room to amounts actually paid for refreshments served after 10:30 p.m. (which was during the floor

show); and it also refused to approve the tax assessed by the Government on 5 per cent of the receipts from patrons of the Ciroette Room. [R. 59-60, 123-124.] We submit that the District Court's decision as to the tax on receipts from the patrons of these rooms is primarily due to an erroneous interpretation of the law.

B. Applicable Statutory Provisions and Other Authorities.

As the cabaret taxes assessed herein cover the period June 1, 1951, to March 31, 1955, the applicable statutory provisions are found in Section 1700(e) of the Internal Revenue Code of 1939 and Sections 4231 and 4232 of the Internal Revenue Code of 1954, Appendix A, *infra*. It will be seen that the provisions in both Codes are substantially the same, and that the portions we are primarily concerned with here are set forth in identical language and provide that there shall be levied, assessed, collected and paid—

> A tax equivalent to 20 per centum of all amounts paid for admission, refreshment, service, or merchandise, at any roof garden, cabaret, or other similar place furnishing a public performance for profit, by or for any patron or guest who is entitled to be present during any portion of such performance. * * *

In interpreting and applying this provision, the District Court refused to read it literally and in taking that position stated [R. 48] that "A literal translation of the above provision would ascribe to Congressional intent a most arbitrary and unreasonable basis on which the tax is imposed." But the court did not give any convincing reasons to support this statement or for its refusal to

apply the statute as written,[3] and we submit that in failing to follow it literally it clearly erred.[4]

When a statute is written in clear and simple language the proper way to determine its meaning is obviously by the language used therein and it is evident that the statutory provision involved here is written in such language. Not only is the sentence structure clear but every word therein is one in common usage and widely understood. Under a long established rule, words in a tax statute must be given their ordinary and commonly accepted meaning. *Deputy v. du Pont,* 308 U. S. 488, 493; *Old Colony R. Co. v. Commissioner,* 284 U. S. 552, 560. Moreover, effect must be given, if possible, to all words and parts of a tax statute so that none will be insignificant or meaningless. *Technicolor Motion Picture Corp. v. Westover,* 202 F. 2d 224, 228 (C. A. 9th). But when these rules of statutory construction are applied here it becomes apparent that the ordinary meaning of the statutory language is necessarily the same as its literal meaning, which the District Court has rejected.

Consequently it is our position that it was the intention of Congress to impose a cabaret tax on all amounts paid for food, refreshment, service or merchandise by or for

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[3]In arguing against the Government's interpretation, the only illustration given at this point in the District Court's opinion [R. 48] is that of afternoon patrons who might stay on for the floor show which usually began about 10:30 p.m. The record does not show that there ever were such patrons and if there were, presumably they would be in the Main Room or lounge where it appears to be conceded that a tax should be imposed on all amounts paid by patrons who remain for the floor show.

[4]We have found nothing in the Congressional reports which would indicate that Congress intended anything but a literal reading of the statute nor did the court below refer to any such reports to support its views as to what the Congressional intent was when the cabaret tax was imposed.

patrons or guests who are entitled to be present during any part of the public performance given at a cabaret for profit. It will be seen from the District Court's opinion that the court rejected the Government's interpretation of the statute largely because it was unwilling to give the words "all amounts" and "entitled to be present" their ordinary and commonly accepted meaning. [R. 53.] We shall discuss this more fully below but we wish to point out here that we know of no valid reason why the court should hesitate to give such meaning to those words.

Of course all of the patrons of the Pavillion and Ciroette Rooms who were attending so-called private parties therein were actually entitled to be present at Ciro's floor show and a tax on all of the receipts from them would add considerably to the total amount of tax due but that is certainly not a valid reason for failing to give words of a statute their true meaning. Moreover in applying the above statutory provision, it has been the Government's policy to include only receipts from patrons who not only are entitled to see the show but who have in fact remained to see it. The Government's position is explained in Rev. Rul. 54-487, 1954-2 Cum. Bull. 376 (Appendix A, *infra*) which provides, in part, as follows:

> The cabaret tax applies to all amounts paid for food, refreshment, service, or merchandise by patrons or guests who are present during any part of the entertainment, even though such patrons or guests make payment for the food, refreshment, service, or merchandise prior to the time the entertainment starts. For the tax to apply, it is not necessary that such patrons or guests be able to witness the entertainment, and partake of food or refreshments at the same time.

> It is held that payments for food, refreshment, service, or merchandise made prior to the beginning of the entertainment in a cabaret, roof garden or other similar place are subject to the cabaret tax imposed by section 1700(e) of the Code, where the patrons or guests by or for whom such amounts are paid remain for any portion of the entertainment afforded. However, the tax does not apply to payments made by or for patrons or guests who leave the establishment prior to the beginning of the entertainment, or who enter and leave during an intermission period, or who enter after the entertainment has ceased.

See also Section 101.13 of Treasury Regulations 43 (Appendix A, *infra*).

We submit that the position taken in the above ruling is a fair and proper one. The statute contains no provision requiring that a patron make his payment for any of the designated items or partake of any refreshments during the time that he is viewing the cabaret's show, and such requirement should not be read into statute. The only statutory conditions, so far as the patron is concerned, are that he make payments and that he is *entitled to be present during part of the public performance.* As indicated, the Government through a liberal interpretation of the statute has included only patrons who are entitled to see the show *and have remained to see it.*

C. Errors in the District Court's Interpretation of the Applicable Statute.

As indicated above, the District Court held that the cabaret tax could be applied to amounts paid for refreshments served after 10:30 p.m. (when the floor show began) to patrons who had been in attendance at one of

the private parties in the Pavillion Room.[5] [R. 123-124.] In so ruling, the District Court must have found that such patrons were "entitled to be present" at a public performance and in that particular connection must have given the words "entitled to be present" their ordinary meaning. But it refused to give that meaning to those words when determining whether to tax payments made by the same patrons of the Pavillion Room for items served prior to the show. However the basis for its refusal was not that it thought payments and eating of food should occur at the same time as viewing of the public entertainment. Indeed it indicated [R. 51] that in some cases the preperformance payments should be taxed. The reason for these seemingly inconsistent views is that the District Court was of the opinion that the taxability of preperformance receipts should be determined by the motives of the patrons (comprising the private parties) in coming to the cabaret. We submit that this is an unwarranted interpretation of the law but as the District Court has repeatedly emphasized the importance of motive we wish to call attention to the following statements in its opinion [R. 53, 55, 56]:

> As noted earlier, *"entitled to be present" cannot be construed literally and must be read in the light of the circumstances of each individual case.* Even assuming arguendo that in view of the removal of the partition at or about 10:30 p.m. there was a public

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[5]Presumably patrons of the Ciroette Rooms were also taxed on amounts paid by them for refreshments during the show but as they had to view the show from the Main Room or lounge, any receipts from them were apparently mingled with receipts from the regular patrons in those rooms. But the District Court held that no preperformance receipts from Ciroette Room patrons were taxable although it was stipulated [R. 161] that 5 per cent did see the show in the Main Room.

performance in regard to the Pavillion Room guests it is not determinative of whether such guests were entitled to be present under the meaning which I have ascribed to such words. The fact that the Pavillion Room parties may have been public when viewed in their entirety is immaterial insofar as it pertains to the pre-performance receipts if it be shown that the main purpose of private groups in engaging the Pavillion Room was other than to be present at the entertainment. * * *

It follows that in the instant case a determination of whether the parties when viewed in their entirety are public or private cannot be conclusive of the ultimate issue presented. Rather, the applicability of the tax is to be *tested by the motivation formulation which I have previously described.* * * *

The crucial determination then, as I see it, is whether the operation of these so-called private parties is so intimately related to the general operation of the Main Room, and the viewing by the Pavillion Room guests of the entertainment at 10:30 p.m. such an integral part of their evening's activities, that it can be reasonably inferred *that the compelling motive in reserving the use of the Pavillion Room was for purposes of seeing Ciro's entertainment.* * * * (Italics supplied.)

From these excerpts, it is obvious that the District Court has ignored the true meaning of the statute and has read into the statute something which was neither included nor intended by Congress, namely, a subjective test as to the motives of patrons who stay for a floor show after attending a private party in some room of a cabaret. Certainly it is apparent that any subjective test would be difficult to make and is not a satisfactory one in the exact field of taxation. At any rate, such a

test should not be required in any tax matter without clear Congressional authority and there is none here. Instead in imposing the cabaret tax, Congress specifically indicated that it should be applicable to all amounts paid for the designated items by or for patrons or guests entitled to be present at a public performance for profit in a cabaret. This clear and exact statutory language makes the determination of the motives of any patron or guest immaterial.

D. The Cases Which the District Court Relied on Do Not Support Its Decision.

This District Court cited three cases which involve the cabaret tax. Two of these will be discussed below under Point IV. The third one is *La Jolla Casa De Manana v. Riddell,* 106 F. Supp. 132 (S. D. Cal.), affirmed by this Court *per curiam,* 206 F. 2d 925. As we shall now point out the facts in the *La Jolla* case are distinguishable but the conclusions reached therein support the Government's position here.

The taxpayer in that case was the owner and operator of a hotel which had accommodations for dancing on its terrace and furnished music for such dancing from about 9 p.m. until midnight. Refreshments were sold at a bar adjoining the terrace and could be obtained until 2 a.m. The taxpayer paid the cabaret tax on all amounts collected from the patrons until midnight but the Government also assessed a cabaret tax on amounts spent at the bar during the period from midnight until 2 a.m. if the patrons making the payments had been present during some portion of the music and dancing. It was held that no tax could be applied to such amounts because the establishment had ceased to be a cabaret after midnight. In explaining its position, the District Court pointed out

that the Government had in effect conceded that there was no cabaret after midnight when it conceded that no tax could be imposed on amounts spent by a patron who had not been present at any portion of the performance before midnight.

In the instant case the District Court indicated that it was using the same reasoning as that employed in the *La Jolla* case but we submit that it failed to recognize the essential difference in the two cases. Obviously in the *La Jolla* case, amounts spent from midnight to 2 a.m. could not entitle any patron to be present at the dancing or to hear the music which had ceased at midnight and for that reason it was held that no tax could be imposed on such amounts. But here the amounts spent by patrons for dinner or other refreshments served at private parties in the Pavillion and Ciroette Rooms actually did permit them to be present at the floor show given in Ciro's Main Room. Indeed if they had not spent such amounts they could not have been present unless of course they had been patrons in the Main Room or lounge, in which case their payments would certainly have been taxed. Thus there is in this case that essential relationship between service of refreshment and the enjoyment of the entertainment which the *La Jolla* case refers to and the facts of this case meet the requirement set out therein, namely "that the payment for the refreshment should operate to entitle the patron to view the entertainment, or participate in the dancing, as the case may be." (P. 135.)

II.

The Decision of the District Court Is Based on Erroneous Conclusions and Should Be Reversed Regardless of Whether Its Interpretation of the Statute is Correct.

We do not of course accept the District Court's interpretation of the applicable statutory provisions but even assuming *arguendo* that its interpretation is correct, we submit that its decision should still be reversed because it reaches conclusions contrary to the evidence and its own findings of fact.

As we have pointed out, the District Court stated in its opinion [R. 52-56] that taxability of preperformance receipts from patrons of the Pavillion and Ciroette Rooms should be determined by the motive of such patrons, and this is also indicated in the court's conclusions of law. The first conclusion is, in substance, that the cabaret tax was not intended to cover preperformance parties by those "whose desire to be present at the public performance was incidental to some more cogent reason for attending the cabaret" and its second conclusion is that the statutory words "entitled to be present" do not apply to the Pavillion Room or Ciroette Room parties "where the main purpose of the parties" was other than to be present at the entertainment. [R. 122-123.] As the District Court then decided that the cabaret tax could not be applied to preperformance payments by patrons of these two rooms, we must of course assume that the court's ultimate conclusion is that the desire of such patrons to attend the cabaret performance was *merely incidental* and not a cogent reason for coming to these parties. We do not agree because the evidence and certain findings of fact show otherwise.

Mrs. Dolores Miller, who handled most of the contracts and preliminary arrangements for banquets at Ciro's testified that it was normal procedure to advise groups requesting the Pavillion Room that they could see the floor show by pulling aside the accordion curtain and that it was the practice of most of the groups to see the show. [R. 306-307.] She also stated that she knew they liked the idea of being able to see the show and the opportunity to do so was "one of the selling features" for holding their parties in the Pavillion Room. [R. 310, 311.]

Four persons who had made arrangements for groups to have parties in the Pavillion Room also testified. Vincent Johnson stated that when making arrangements for his group's party, he was told that at floor show time the curtain would be drawn back and that the group could see the show, that this was done and that 100 per cent of his group (numbering 85) stayed to see the show. [R. 248.] The other three witnesses gave similar testimony and explained as to the number who remained to see the show that in each instance it was almost 100 per cent. [R. 252-253, 264, 277.] At the close of this testimony, the parties herein then filed a stipulation stating that it was agreed if representatives of each of the remaining 300 Pavillion Room parties were called as witnesses, each would give answers similar to those given by the four witnesses who had appeared. But this stipulation also pointed out that there were about six groups which had regular business meetings in the Pavillion Room and did not see the show. [R. 278-280.] Three witnesses who arranged for parties in the Ciroette Room testified that they too had been given the opportunity to see the floor show and that a considerable number had done so. [R. 294, 296-297, 302-305.]

Further evidence as to the concern of private parties about seeing Ciro's floor show is found in the Government's Analysis of Joint Exhibit 2-B (attached to the Stipulation). [R. 32-35.] This is an analysis of the comments appearing in the written contracts made by Ciro's with representatives of groups holding parties in the Pavillion Room. It will be seen that most of the comments therein were about the show, that both Ciro's and the representatives of the various groups expected most of the groups to see the show, and that in 257 instances the groups were advised by Ciro's that the price of drinks would be raised from 75 cents at dinner time to 90 cents at show time.

The District Court ignored some of this uncontroverted evidence but it did make several findings of fact which support our contention that the desire to see the floor show was not an incidental matter but was a cogent reason for going to Ciro's. These findings include the following:

The patrons attending the dinner in the Pavillion Room expected to be able to see the entertainment in the Main Room, it being the understanding, whether committed to writing or not, that the so-called private parties would be afforded this privilege. [Finding IX, R. 115-116.]

Ciro's was a famous night club which widely advertised its entertainment and in its advertising Ciro's not only offered the facilities of the Ciroette and Pavillion Rooms but indicated that as one of the several inducements for such gatherings in those rooms was the opportunity to view the floor show. [Findings XII and XIII, R. 116.]

While there was some variation in the way the 304 parties in the Pavillion Room were conducted, at approxi-

mately 10:30 p.m. the separation between that room and the Main Room was usually removed so as to enable the groups to view the floor show in the Main Room. [Finding VIII, R. 115.]

The taxpayer permitted members of private parties using the Ciroette Room to see the entertainment at 10:30 p.m. and some 5 per cent did in fact avail themselves of this opportunity. [Finding XXVI, R. 120.]

We submit that the above evidence and findings of fact established that the persons who held private parties at Ciro's were primarily interested in seeing the floor show. Of course they also liked the privacy that Ciro's room afforded them and the other facilities therein but the fact that the widely advertised floor show was being offered them was clearly a matter of major importance in each group's choice of a place to hold the parties. Obviously any of the persons attending these parties may also have had other motives for coming, such as the desire to see friends or to advance business connections but the evidence does not show what these motives were, if they existed, nor does it show which persons may have had them. However the record does contain uncontroverted evidence that the persons attending the private parties in the Pavillion Room expected to see the floor show, that most of them did stay to see it and that their representatives in arranging for the parties were assured that they could see the show. We submit that this is sufficient to satisfy the test even under the District Court's interpretation of the law.

In concluding otherwise, the District Court seems to have been largely influenced by the difference in the physical properties of the Main Room and the Pavillion Room and in the way they were operated. Thus it pointed

out that they had different furnishings, menus, prices and services. [R. 118.] However we fail to see how such differences can be material either under our interpretation or that of the District Court. And it should be noted in this connection that although the differences in these rooms were held to be important factors when considering the preperformance payments by patrons of the Pavillion Room, the District Court held that when the partition between that room and the Main Room was removed at show time "no distinction between the two rooms is warranted" and that "the Pavillion Room guests did observe and participate in the public performance in common with other patrons in the Main Room." [R. 119.]

As we have indicated, the physical differences in these two rooms can not be decisive of the issue here. Instead the essential thing under our interpretation of the statute is that patrons at private parties in the Pavillion Room and the Ciroette Room were actually entitled to be present and the evidence shows that a large number of them did stay to see the show. And under the District Court's interpretation, the record shows that that test has been met since a cogent reason for selecting Ciro's was its floor show. Certainly it can not be said that Ciro's floor show was merely an incidental reason as the District Court seems to have concluded. The word incidental, as defined in Webster's International Dictionary (Abridged 2nd ed.), means "happening as a chance or undesigned feature of something else, casual hence not of prime concern." We submit that the floor show was not "an undesigned feature" of the private parties at Ciro's but it was of prime concern and a major reason why Ciro's was chosen. In holding otherwise, the District Court has reached a decision contrary to the evidence and its own findings.

III.

The District Court Erred in Failing to Enter Judgment for the Full Amount of Taxes Assessed Inasmuch as the Taxpayer Failed to Overcome the Presumption of Correctness Attaching to the Assessment by Producing Proper Records or by Any Other Proof.

The Government assessed a cabaret tax on 94 per cent of the receipts attributed to the 304 private parties in the Pavillion Room involved herein [R. 114-115] and also assessed the same tax on 5 per cent of the receipts from the Ciroette Room during the period involved here. [R. 120.] We contend that under the District Court's interpretation of the statute as well as under that of the Government, judgment should have been given for the full amount of taxes assessed. It has long been established that a presumption of correctness attaches to a tax assessment and that the taxpayer against whom the assessment is made has the burden of overcoming such presumption. *United States v. Rindskopf,* 105 U. S. 418; *San Joaquin Brick Co. v. Commissioner,* 130 F. 2d 220 (C. A. 9th); *Crook v. United States,* 30 F. 2d 917 (C. A. 5th); also see *Maroosis v. Smyth,* 187 F. 2d 228 (C. A. 9th).

The taxpayer produced no evidence to show that the assessment here was in any way incorrect. Furthermore the taxpayer kept no records showing what proportion of the persons who attended the parties in the Pavillion Room stayed for the floor show or dancing.[6] [R. 114, 224.] But the taxpayer should have kept such records. Section 1720 of the Internal Revenue Code of 1939 (Appendix A, *infra*) provides that a taxpayer shall keep the records

---

[6]As to the receipts from the Ciroette Room there are also no records but it has been stipulated that if any tax is due, it can be computed on the five per cent basis used by the Government. [R. 120.]

which the Commissioner, with the approval of the Secretary, may from time to time prescribe, and what the Commissioner has prescribed is set forth in Section 101.32 of Treasury Regulations 43 (Appendix A, *infra*) which requires the taxpayer to keep adequate records (1) as to the operations for each day on which public performances are held, (2) as to the receipts from patrons entitled to be present during any part of the performance and (3) as to the taxes due. This regulation also provides that these records shall contain sufficient information to enable the Commissioner to determine whether the correct amount of taxes has been paid, that they shall be available at all times for inspection by Internal Revenue Agents and that they shall be maintained for a period of at least four years from the date that the tax becomes due. As the taxpayer has not met these requirements and has failed to produce any evidence to show that the assessment was in any way incorrect, judgment should have been entered against him for the full amount of tax assessed.

IV.

The District Court Erred in Holding With Respect to the "Closed House" Parties That the Payments Received From the Patrons of Such Parties Did Not Entitle Them to Be Present During a Public Performance for Profit and in Failing to Hold That Such Payments Were Subject to the Cabaret Tax.

Part of the deficiency assessment involved here consists of a tax on all amounts paid for admission, refreshments, service or merchandise on twenty evenings when all facilities of Ciro's were reserved by and for the members of a particular organization. As the District Court pointed out [R. 60-61] the Government's position as to the taxability

of such receipts is set forth in the Special Ruling of August 31, 1949, 1950 C. C. H., par. 6053, which reads in part as follows:

> Where a private organization arranges to hold an affair in a room at a hotel which normally is operated as a cabaret and the affair is held under such circumstances that the hotel furnishes practically the same services including entertainment, during the same hours that the room is operated as a cabaret, the arrangements made by the private organization are regarded as a mere reservation of tables. In such case, the Bureau holds that the room is operated as a cabaret on such occasions, even though the patronage is limited to the members, together with the guests of the private organization, and the private organization furnishes entertainment in addition to that furnished by the hotel. The cabaret tax then applies to the payment made by the private organization to the hotel.
>
> * * *
>
> Where a private organization holds a dinner in a room at a hotel, under such circumstances that the hotel does not furnish any entertainment but the private organization does provide dancing facilities for the persons attending by hiring an orchestra, or furnishes other entertainment, cabaret tax does not apply to any amount paid in connection with the affair.

We submit that this is a proper interpretation of the statute and that the key to taxability of receipts from "Closed House" parties is the cabaret's furnishing a public performance for profit. Thus it is the Government's position here that since these parties were given during the usual cabaret hours and on nights when Ciro's would be open and operating, they were public within the meaning of the statute and the only factor which could prevent

the imposition of a tax on payments connected therewith would be that the entertainment had been furnished by the private organizations rather than by Ciro's.

The District Court said that it would not pass on the correctness of the above ruling but it did make the test therein the basis for its decision here for after pointing out that no court had yet passed on the ruling, it said that even assuming its correctness, the Government could not prevail on this issue because the organizations which gave the parties at Ciro's contracted for their own entertainment and music. [R. 61-62.] We submit that the District Court was in error in reaching that conclusion since it is contrary to the evidence.

As the District Court found [R. 121], the show and the orchestras usually provided for the "Closed House" parties were the same as those regularly scheduled by Ciro's at the time of the parties. But we can not accept the court's finding [R. 121] that the private organizations contracted for their own entertainment and music.

Mrs. Dolores Miller who handled the preliminary arrangements for Ciro's admitted that in a letter about a party given on March 13, 1952, she offered the regular show and orchestra at Ciro's and that at such time she was acting as a go-between between the entertainers and groups who were arranging for "Closed House" parties. [R. 319-320.] Also see testimony about letter dated June 6, 1952, which also indicated that Mrs. Miller was making arrangements for the group's entertainment. [R. 322-323.] Moreover, although Mrs. Miller testified that

she did not have anything to do with arranging entertainment for such parties later on, letters dated February 17, 1953, October 26, 1953, December 1, 1953, and June 11, 1954, show that the groups involved were not only requesting Ciro's regular orchestra and show but such letters also indicate that Mrs. Miller was actually making the arrangements. [R. 324-326.]

Our position is further supported by the testimony of Mr. Warren Penn, who had made the arrangements for one of the "Closed House" parties and who stated that the entertainment his organization had was furnished by Cugat and his group, they being Ciro's regular entertainments at that time. Attention is called particularly to the following excerpt from Mr. Penn's testimony [R. 330-331]:

> Q. You never made any arrangements with Mr. Cugat with regard to this show?
>
> A. No, I didn't talk to him.
>
> Q. Or with any theatrical agents for Mr. Cugat?
>
> A. No, none whatever.
>
> Q. All your arrangements were made with the management, that is the personnel of Ciro's?
>
> A. Yes, with Johnnie Oldrate.
>
> Q. To whom did you give the check made to Mr. Cugat?
>
> A. I had the check made out and Mr. Oldrate asked me if I had a check for the money, and I said: "Yes, I am going to give it to Mr. Cugat in a minute."
>
> He said, "Give it to me and I will give it to him." So I gave him the check and I guess he gave it to them.

We also call attention to the testimony of Mr. David S. Greenberg. He arranged for a "Closed House" party at Ciro's on December 23, 1953, and stated that he made his arrangements with Mrs. Miller. [R. 336-337.] Then he testified as follows [R. 340-341]:

> Q. What arrangements were made with Ciro's with respect to the entertainment?
>
> A. Well, we just asked them for the regular show.
>
> * * * * * * * *
>
> Q. How did you arrive at the amount the entertainers were to be paid, was that told to you by Ciro's?
>
> A. That was told to us the evening of the affair, yes.

Mr. Sol Hirschhorn, who arranged for a "Closed House" party early in 1955 testified that he told Mrs. Miller he wanted Ciro's entertainment, that at the time arrangements were made for the party Mrs. Miller did not know who the entertainers would be but said she would be glad to help him, that his group was to pay the entertainers direct and that he was told either by Mrs. Miller or by the maitre d' at Ciro's how to divide the amount due to various entertainers. [R. 333-335.]

From this evidence, it is apparent that the various organizations which had "Closed House" parties used the same orchestra and floor show that Ciro's was offering to the public and that the arrangements by these groups amounted to no more than a reservation of all the tables. Thus we submit the District Court was in error in not

finding that Ciro's had in fact arranged for the entertainment at these "Closed House" parties and in not holding that the payments received therefrom were subject to the cabaret tax.

As the taxpayer has opposed the application of the above ruling to this issue we wish to explain and answer the contention advanced by him in the District Court. The taxpayer argued that this ruling is contrary to those cases which determine the applicability of the cabaret tax on the basis of whether the parties are public or private and cited *United States v. Lambeth,* 176 F. 2d 810 (C. A. 9th), and *Naylor v. United States,* 102 F. Supp. 309 (S. D. Cal.). We do not agree that either of those cases is applicable here as both involved private clubs. Obviously the clubs therein would not be furnishing their members and guests of their members public performances for profit. Therefore the parties involved in those cases were the same as if they had been held in the member's own homes. It should also be noted that in the *Lambeth* case this Court refused to overturn the lower court's finding of fact that the taxpayer had not been serving the public. And in the *Naylor* case the issue was whether the alleged club was in fact a *bona fide* club and as the court found that it was, there could then be no question as to the music and dancing therein constituting a private rather than a public performance.

Conclusion.

The judgment of the District Court was erroneous insofar as it failed to order the taxpayer to pay the entire amount of taxes and interest asserted and should be reversed to that extent.

Respectfully submitted,

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January, 1959.

APPENDIX A.

Internal Revenue Code of 1939:

SEC. 1700. TAX.

There shall be levied, assessed, collected, and paid—

* * * * * * * *

(e) [as amended by Sec. 622, Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 404(a), Revenue Act of 1951, c. 521, 65 Stat. 452, and Section 201(c), Excise Tax Reduction Act of 1954, c. 126, 68 Stat. 37] *Tax on Cabarets, Roof Gardens, Etc.*—

(1) *Rates.*—A tax equivalent to 20 per centum[7] of all amounts paid for admission, refreshment, service, or merchandise, at any roof garden, cabaret, or other similar place furnishing a public performance for profit, by or for any patron or guest who is entitled to be present during any portion of such performance. The term "roof garden, cabaret, or other similar place" shall include any room in any hotel, restaurant, hall, or other public place where music and dancing privileges or any other entertainment, except instrumental or mechanical music alone, are afforded the patrons in connection with the serving or selling of food, refreshment, or merchandise. In no case shall such term include any ballroom, dance hall, or other similar place where the serving or selling of food, refreshment, or merchandise is merely incidental, unless such place would be considered, without the application of the preceding sentence, as a "roof garden, cabaret, or other similar place." A performance shall be regarded as being furnished for profit for purposes of this section even though the charge made for admission, refreshment, service, or merchandise is

---

[7]The rate of tax was changed to 20 per cent by Section 3(a), public Debt Act of 1944, c. 240, 58 Stat. 272, which amended Section 1650 of the 1939 Code, a section specifying war tax rates.

not increased by reason of the furnishing of such performance. * * *

* * * * * * * *

(26 U. S. C. 1952 ed., Sec. 1700.)

SEC. 1720. RECORDS, STATEMENTS, AND RETURNS.

Every person liable to any tax imposed by this chapter, or for the collection thereof, shall keep such records, render under oath such statements, make such returns, and comply with such rules and regulations, as the Commissioner, with the approval of the Secretary, may from time to time prescribed.

(26 U. S. C. 1952 ed., Sec. 1720.)

Internal Revenue Code of 1954:

SEC. 4231. IMPOSITION OF TAX.

There is hereby imposed:

* * * * * * * *

(6) *Cabarets.*—A tax equivalent to 20 percent of all amounts paid for admission, refreshment, service, or merchandise, at any roof garden, cabaret, or other similar place furnishing a public performance for profit, by or for any patron or guest who is entitled to be present during any portion of such performance. The tax imposed under this paragraph shall be returned and paid by the person receiving such payments. * * *

(26 U. S. C. 1952 ed., Supp. II, Sec. 4231.)

SEC. 4232. DEFINITIONS.

(a) *Admission.*—The term "admission" as used in this chapter includes seats and tables, reserved or otherwise, and other similar accomodations, and the charges made therefor.

(b) *Roof Garden, Cabaret or Other Similar Place.*—The term "roof garden, cabaret, or other similar place,"

as used in this chapter, shall include any room in any hotel, restaurant, hall, or other public place where music and dancing privileges or any other entertainment, except instrumental or mechanical music alone, are afforded the patrons in connection with the serving or selling of food, refreshment, or merchandise. In no case shall such term include any ballroom, dance hall, or other similar place where the serving or selling of food, refreshment, or merchandise is merely incidental, unless such place would be considered, without the application of the preceding sentence, as a "roof garden, cabaret, or other similar place."

(c) *Performance for Profit.*—A performance shall be regarded as being furnished for profit for purposes of section 4231 (6) even though the charge made for admission, refreshment, service, or merchandise is not increased by reason of the furnishing of such performance.

(26 U. S. C. 1952 ed., Supp. II, Sec. 4232.)

Treasury Regulations 43 (1941 ed.):[8]

Sec. 101.13 [As amended by T. D. 5385, 1944 Cum. Bull. 637, and T. D. 5349, 1944 Cum. Bull. 639]. *Basis, rate, and computation of tax.*—The tax imposed by section 1700(e), as amended, applies to all amounts paid for admission, refreshment, service, and merchandise, at any roof garden, cabaret, or other similar place furnishing a public performance for profit, by or for any patron or guest who is entitled to be present during any portion of such performance. The tax is at the rate of 20 per cent of the total amounts so paid.

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[8]These Regulations were also made applicable to Sections 4231 and 4232 of the 1942 Code, *supra,* by T. D. 6091, 1954-2 Cum. Bull. 47.

Charges collected prior to commencement of a performance are not taxable with respect to such performance, if the patron does not remain for any part of the performance.

The liability for the tax is imposed upon the person receiving payment of the charges mentioned, and the tax must be paid by such person regardless of whether collected from the patron either as a separate charge or by being included in the amounts charged for admission, refreshment, service, and merchandise.

* * * * * * * * *

Sec. 101.14 [As amended by T. D. 5192, 1942-2 Cum. Bull. 249, and T. D. 6007, 1953-1 Cum. Bull. 412]. *Scope of tax.*—The term "roof garden, cabaret, or other similar place" includes any room in any hotel, restaurant, hall, or other public place where music and dancing privileges or any other entertainment except instrumental or mechanical music alone, are afforded the patrons in connection with the serving or selling of food, refreshment, or merchandise, except that after 10:00 a.m. November 1, 1951, such term does not include any ballroom, dance hall, or other similar place where the serving or selling of food, refreshment, or merchandise is merely incidental, unless such place would otherwise be considered as a roof garden, cabaret, or other similar place. The exception with respect to ballrooms, dance halls, or other similar places, applies only to such of those establishments which are operated primarily to furnish music and dancing privileges and where the serving or selling of food, refreshment, or merchandise constitutes in fact an incidental or subsidiary service in relation to the furnishing of music and dancing privileges.

A public performance furnished at a roof garden, cabaret or other similar place shall be regarded as being

furnished for profit for purposes of this section even though the charge made for admission, refreshment, service, or merchandise is not increased by reason of the furnishing of such performance.

Where music, whether by an orchestra, a mechanical device, or otherwise, and a space in which the patrons may dance is furnished in the dining room of a hotel, or in a restaurant, bar, etc., the entertainment constitutes a public performance for profit at a roof garden, cabaret, or similar place, and the payments made for admission, refreshment, service, and merchandise are subject to the tax.

Amounts paid for refreshment, service, or merchandise in a room which is entirely separate from the room in which entertainment is furnished are not subject to tax, provided that the patrons in such separate room may not witness the entertainment and any door in the wall or partition separating the two rooms remains closed during the period of the entertainment except when persons pass from one room to the other.

* * * * * * * * *

Sec. 101.32 [As amended by T. D. 5385, *supra,* and T. D. 5673, 1948-2 Cum. Bull. 165]. *Records—Admissions.*—* * *

* * * * * * * * *

(B) *Admissions subject to tax under section 1700(e), as amended.*—Every person required to pay the tax imposed by section 1700(e), as amended, on charges made for admission, refreshment, service, and merchandise, at any roof garden, cabaret, or other similar place furnishing a public performance for profit, must keep or cause to be kept adequate and sufficient records with respect to the operation for each day on which such public performances are held showing (1) the receipts from charges made for admission, refreshment, service, and

merchandise paid by all patrons entitled to be present during any part of the performance; and (2) the tax due.

Where the passing on of the tax is evidenced by the use of waiters' checks or bills which show the tax as a separate item or by the use of a cash register which records the tax under separate symbols on the cash register tape, as provided by method (1) or (2) included in paragraph four of section 101.13, the total receipts from patrons (exclusive of tax) and the total taxes passed on to them as disclosed by the waiters' checks or bills or the cash register tapes for each day should be entered in the daily record. Where the tax is not shown as a separate item but the passing on of the tax is evidenced by the use of signs or by statements on the menus, as provided by method (3) included in paragraph four of section 101.13, the gross receipts for each day should be entered in the daily record.

Such records shall contain sufficient information to enable the Commissioner to determine whether the correct amount of tax has been paid. The records shall at all times be open for inspection by internal revenue officers, and shall be maintained for a period of at least four years from the date the tax became due.

Where the passing on of the tax to the patrons is evidenced by entries on waiters' checks or bills or by the use of a cash register, the waiters' checks or bills or the cash register tapes must be kept by the establishment for a period of not less than six months.

(C) *Duplicate returns.*—Subject so far as applicable to the conditions prescribed as to other records required by this section each person required to keep such other records shall also retain in his records the duplicate returns required by section 101.33.

Rev. Rul. 54-487, 1954-2 Cum. Bull. 376:

Regulations 43, Section 101.13: Basis, rate, and computation of tax.

Advice is requested concerning the application of the cabaret tax imposed by section 1700(e) of the Internal Revenue Code of 1939 to amounts paid for food and refreshment served in a cabaret under the following circumstances.

In the instant case, a cabaret serves full course dinners between the hours of 5 p.m. and 9 p.m. After that time all food and refreshments are served on an a la carte basis. Entertainment in the cabaret begins at 9:30 p.m. Some of the customers call for and pay their checks before the entertainment begins, but remain to finish their meals and are able to witness all or part of the entertainment.

Section 1700(e) of the Code imposes a tax equivalent to 20 percent of all amounts paid for admission, refreshment, service, or merchandise at any roof garden, cabaret, or other similar place furnishing a public performance for profit, by or for any patron or guest who is entitled to be present during any portion of such performance. The term "roof garden, cabaret, or other similar place" includes any room in any hotel, restaurant, hall or other public place where music and dancing privileges or any other entertainment except instrumental or mechanical music alone are afforded the patrons in connection with the serving or selling of food, refreshment, or merchandise.

The cabaret tax applies to all amounts paid for food, refreshment, service, or merchandise by patrons or guests who are present during any part of the entertainment, even though such patrons or guests make payment for the food, refreshment, service, or merchandise

prior to the time the entertainment starts. For the tax to apply, it is not necessary that such patrons or guests be able to witness the entertainment, and partake of food or refreshments at the same time.

It is held that payments for food, refreshment, service, or merchandise made prior to the beginning of the entertainment in a cabaret, roof garden or other similar place are subject to the cabaret tax imposed by section 1700(e) of the Code, where the patrons or guests by or for whom such amounts are paid remain for any portion of the entertainment afforded. However, the tax does not apply to payments made by or for patrons or guests who leave the establishment prior to the beginning of the entertainment, or who enter and leave during an intermission period, or who enter after the entertainment has ceased.

APPENDIX B.

Exhibit	Identified	Offered	Received
Plaintiff's Exhibit 1	R. 131	R. 155	R. 155
" " 2	R. 131	R. 155	R. 155
" " 3-A	R. 131	R. 155	R. 38, 170
" " 3-B	R. 131	R. 155	R. 155
" " 3-C	R. 131	R. 155	R. 155
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" " 4-B	R. 131	R. 155	R. 156
" " 4-C	R. 131	R. 155	R. 156
" " 5	R. 156	R. 156	R. 157
" " 6	R. 167-168	R. 167	R. 168
" " 6-A	R. 193	R. 193	R. 193
" " 7	R. 183	R. 183	R. 183
" " 8	R. 193	—	—
" " 9	R. 346	—	—
Defendant's Exhibit A	R. 226	R. 227	R. 227
" " B	R. 247	R. 247	R. 247
" " C	R. 251	—	—
" " D	R. 262	—	—
" " E	R. 265	R. 265	R. 266
" " F	R. 276	R. 276	R. 276
" " G	R. 279	R. 278	R. 40, 280
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" " H-1	R. 283	R. 283	R. 284
" " I	R. 303	R. 305	R. 305
" " J-1 through J-9	R. 318	R. 326	R. 326
" " K	R. 327-328	R. 328	R. 328
" " L	R. 333	R. 333	R. 333
" " M-1 through M-3	R. 335	R. 335	R. 335
" " N-1 and N-2	R. 335	R. 336	R. 336
" " O	R. 338	R. 339	R. 339
" " P	R. 339	R. 339	R. 42

No. 16,106

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant,

vs.

HERBERT D. HOVER, Doing Business as Ciro's,

Appellee.

On Appeal From the Judgment of the United States District Court for the Southern District of California.

BRIEF FOR THE APPELLEE.

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MAR - 2 1959
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No. 16,106

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UNITED STATES OF AMERICA,

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HERBERT D. HOVER, Doing Business as Ciro's,

Appellee.

On Appeal From the Judgment of the United States District Court for the Southern District of California.

BRIEF FOR THE APPELLEE.

Jurisdiction.

The District Court had jurisdiction of this matter under 28 U. S. C. A., Sec. 1346. This Court has jurisdiction under 28 U. S. C., Sec. 1291.

Statutes Involved.

Appellant has set out the pertinent statutes and regulations in Appendix "A" to its opening brief.

Statement.

Appellant has given us most of the pertinent facts in its opening brief; however, it might be helpful to the Court to restate a few of the facts. The Government assessed cabaret taxes against appellee in the amount of

$67,660.62. Because of a clerical error, appellee has underpaid his cabaret taxes by $992.00, which amount is not in dispute. By stipulation it was agreed that $5,200.63 represented the tax on food, refreshment or merchandise served to Pavillion Room patrons subsequent to 10:30 p.m., if the tax were applicable. The Court gave Judgment for the Defendant in the amount of $7,463.86 which included the adjustment for the clerical error and the $5,200.63 cabaret tax after 10:30 p.m. with adjustments as shown on page 87 of the record.

Pavillion Room.

As appellant has stated, Ciro's is a famous night club located on Sunset Boulevard in Los Angeles. Three issues are involved in this proceeding: the taxability of receipts from Ciro's (1) Pavillion Room; (2) Ciroette Room, and (3) "closed house parties" which took over the entire club for the exclusive use of private organizations when Ciro's was closed to the public. The Pavillion Room is located in a separate building which was added to the Ciro establishment some years after the original structure was built. The Pavillion Room is located adjacent to the lounge and is separated from it by a movable wall and thick soundproof curtain. The floor of the Pavillion Room is slightly above that of the lounge which is between the Main Room and the Pavillion Room. The Pavillion Room was used primarily to accommodate private organizations which reserved the room for the evening for the exclusive use of their members. On occasion, however, part of the Pavillion Room was used for overflow crowds. In issue in this proceeding is the taxability of services, food and refreshments served to 304 private parties in the Pavillion Room. These parties normally commenced around 7:00 p.m. and the dinner would usually be com-

pleted before 9:30 or 10:00 p.m. On some occasions the movable wall would be moved back at 10:30 p.m. when the floor show began. Prior to this, the private organization would have paid the tab for the dinner and the waiters would have departed, leaving the dishes on the table. With respect to the dinners served in the Pavillion Room, there were some 25 basic differences between the method of operation there and that carried on in the Main Room. For example, the table set-up was different; there was no parking fee; the prices of drinks were different; the waiters served all evening until closing; the waiters worked on a different hourly basis; the menu was prearranged in the Pavillion Room, whereas service was a la carte in the Main Room; prices in the Main Room were 40% to 60% higher than in the Pavillion Room; service was different in that vegetables were served in different dishes in the Main Room but usually on the same plate in the Pavillion Room; payment was made for all tables on one check in the Pavillion Room but in the Main Room payment was made for the tables individually; and dinners were compulsory to patrons in the Pavillion Room but not in the Main Room. In order to see the floor show, patrons in the Pavillion Room would have to move up front to get a clear view. The Pavillion Room had its own separate entrance although ingress and egress was possible by way of the lounge. The rest rooms were shared in common with the Main Room although entrance could be made from the Pavillion Room itself.

Ciroette Room.

The Ciroette Room, like the Pavillion Room, was used to accommodate private parties. It is located on the second floor of Ciro's and members of the Ciroette private parties would have to go down a flight of stairs and pass

through two doorways in the Main Room in order to view the floor show. It was stipulated that 5% of the Ciroette patrons did, in fact, view the floor show so if any cabaret tax were due it would be computed on the basis of 5% of the Ciroette receipts. The same basic difference between services in the Ciroette Room and the Main Room as were mentioned with respect to the Pavillion Room, apply to the Ciroette Room.

Closed House Parties.

The Government assessed a cabaret tax on the receipts from twenty "closed house" private parties held during the period involved on the ground that engaging the whole of Ciro's by the private organization was "regarded as a mere reservation of tables." (App. Br. 33.) On these twenty nights Ciro's was closed to the public, the complete establishment having been engaged by private organizations.

Summary of Argument.

Pavillion Room.

The Trial Court correctly held that the private parties in the Pavillion Room did not constitute a public performance for profit prior to 10:30 p.m. when the folding wall was removed and therefore no cabaret tax was incurred on charges for food, refreshment and services prior to 10:30. This is in direct conformity to the holding of this Court in *La Jolla Casa de Manana v. Riddell,* 106 Fed. Supp. 132, aff'd *per curiam,* 206 F. 2d 925. It was there held that the Casa de Manana was not a cabaret from 12:00 p.m. to 2:00 a.m. after the entertainment had ceased despite the fact that post-midnight patrons had enjoyed the entertainment before midnight. The District Court could not have applied the *Casa de Manana*

case in any other way because the same basic issue was involved in the pre-entertainment period that was involved in the *Casa de Manana* post-entertainment period. Obviously, patrons of the Casa de Manana were "entitled to be present" at the entertainment because it was undisputed that some of the patrons who remained after midnight (which was the basis of the assessment) had actually been present at the entertainment. Despite the literal wording of the statute, this Court held that patrons who enjoyed the entertainment and were therefore "entitled to be present" at the entertainment were nevertheless not subject to tax because at 12:00 midnight the Casa de Manana ceased to be a cabaret. Consistently with this the Trial Court held in the instant case that private parties in the Pavillion Room prior to 10:30 p.m. did not constitute a cabaret. The District Court having decided as a fact that these private parties did not constitute a cabaret, this Court should not set aside such a finding if there is any substantial evidence to support it. (Rule 52(a), F. R. C. P.)

Ciroette Room.

The above argument applies with even greater force to the Ciroette Room which is on the second floor of Ciro's. As the District Judge stated in his Opinion ". . . the reasons for denying the tax on pre-performance receipts in the Pavillion Room are even more potent here in view of the obvious remoteness of the Ciroette Room. . . ."

Closed House Parties.

The informal Treasury ruling set out at page 33 of Appellant's Brief is so absurd on its face that this Court should hold it to be invalid. To say that the exclusive engagement of a complete establishment such as Ciro's for a night by a private organization is to be "regarded as a mere reservation of tables" is the same as saying the

one who rents a house is merely reserving the chairs, beds, tables and other furnishings therein. In any event, the regulation itself applies only to an affair held "in a room at a hotel." Certainly Ciro's cannot be regarded as a room in a hotel. Furthermore, the District Court held as a fact that Ciro's did not furnish the entertainment and therefore the regulation by its own terms could not apply. That is, the District Court did not pass on the validity of the regulation but decided that the facts of the case did not bring Appellee within the terms of the regulation. This Court, in view of the evidence adduced, should not reverse any such finding of fact as being "clearly erroneous."

ARGUMENT.

Appellant's main thesis appears to be that the District Judge failed to give a literal meaning to the words in Section 1700(e) of the Internal Revenue Code and has used a subjective test in determining taxability. At the outset it should be emphasized that the Government itself does not interpret the words of the Code literally and this Court in the *La Jolla Casa de Manana* case[1] demonstrated the impossibility of ascribing to some of the words their ordinary meaning. The phrase "entitled to be present" is the one most responsible for the ambiguity of this section. The Treasury in its own regulations holds that this phrase does not mean what it says. In Rev. Rul. 54-487, 1954-2 Cum. Bul. 376 (Regs. 43, Sec. 101.13) it is stated:

> "It is held that payments for food, refreshment, service or merchandise, made prior to the beginning of the entertainment in a cabaret, roof garden or other similar place, are subject to the cabaret tax imposed by §1700(e) of the Code where the patrons

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[1]106 Fed. Supp. 132, affd. *per curiam,* 206 F. 2d 925.

> or guests by or for whom such amounts are paid remain for any portion of the entertainment afforded. However, *the tax does not apply to payments made by or for patrons or guests who leave the establishment prior to the beginning of the entertainment, or who enter and leave during an intermission period, or who enter after the entertainment has ceased.*" (Emphasis supplied.)

Thus, the Commissioner by his own regulations concedes that he cannot interpret the words "entitled to be present" in the ordinary sense. That is, the test of taxability is whether or not the patron was *actually* present during the entertainment and not whether he was *entitled* to be present.

As more fully explained later herein the legislative history of Section 1700(e) shows that the Congress intended the word "entitled" to mean *presently* entitled to view the entertainment, not entitled to be present in the past or in the future. And as the District Judge said in the *Casa de Manana* case (p. 135)

> "if a patron purchased refreshments during the progress of the dancing, he could not avoid the tax by electing to leave without dancing because he was *entitled* to be present during a portion of such performance." (Italics in original.)

As further explanation the Court said:

> "It is clear that Congress evidenced *an essential unity between the service of refreshment and the enjoyment of the entertainment.* The reason for this unity is the reason for the tax itself: that the payment for the refreshment should operate to entitle the patron to view the entertainment, or participate in the dancing, as the case may be." (Emphasis supplied.)

If the word "entitled" were used in its ordinary sense, it would mean that the cabaret tax would apply to payments made for lunch even though the entertainment did not begin until 10:30 p.m. because the patron would be entitled to view the entertainment if he stayed in the establishment throughout the afternoon and evening.

As stated above, the fact that the words "entitled to be present" are to be considered in terms of the "essential unity between the service of refreshment and the enjoymnt of entertainment" is borne out by the legislative history of Section 1700(e) itself. The predecessor of Section 1700 (e) was part of a Revenue Act imposing an *admissions* tax. It was enacted in 1917 (40 stat. 318) as an emergency measure to help finance our part in World War I. The Section was amended several times but basically it has retained its identity as an admissions tax provision. The report of the House Ways and Means Committee (No. 45, 65th Cong. 1st Sess. p. 8) states that a tax is being levied equivalent to 10% of the "amount paid for admission to any place to which admission is charged." The tax was applied to admissions to theatres, circuses, cabarets, ball games and similar entertainments. Administrative difficulties were encountered in applying the tax to cabarets because admission charges were generally not made and the tax was basically an admissions tax. Under Treasury Rulings a breakdown of charges was made so as to ascertain what portion could be attributed to the admission price. Then in 1919 the Act was amended to incorporate various rulings of the Treasury Department. The Act, as amended, continued to impose an admissions tax. In order to apply the tax to cabarets under the Code provision imposing the admissions tax, the Treasury computed the tax on the *difference* between the regular price for refreshments and the cabaret price; for example, if

the bar price of a drink was 15¢ (remember, this is 1917) and the cabaret price was 50¢, the tax would apply to the difference of 35¢ on the theory that this was the "admission" charge. (See hearings on H. R. 4280, Revenue Bill of 1917 quoted in *Gear v. Birmingham,* 88 Fed. Supp. 189 at 196.) Accordingly, if there was an increase in price during the public performance, the tax would apply to the increase. The original Act as amended, became part of the Internal Revenue Code of 1939 as Section 1700(e). Because of the difficulty of its administration, the section was amended in 1949 so that a 5% tax was imposed on the *total charges.* However, it did not change the base on which the tax was applied which was on sales made during the period there was a *public performance for profit.* The tax was increased to 20% in 1944.

It is clear from the legislative history that the cabaret tax was intended by Congress to apply to purchases of food and beverage only "while the floor show is in progress." See for example, the statement in the Senate Report accompanying the Revenue Act of 1942 (77th Cong., 2nd Sess., Report 1683, p. 79):

> ". . . In order to allay possible questions under the present statute, the amendment specifies that the tax, levied on *amounts paid by or for any patron or guest entitled to be present during any portion of the performance shall be applicable,* although no increase is made in the charges for admission, refreshment, service, or merchandise by reason of the furnishing of the performance. Thus the tax will be collected although a cabaret does not increase its prices for food or beverages *while its floor show is in progress.* The amendment confirms the Treasury Department's interpretation of the present statute by stating that the tax is applicable in the case of any room in any

hotel, restaurant, hall, or other public place *where music and dancing privileges or any other entertainment,* except instrumental or mechanical music alone, *are afforded the patrons in connection with* the serving or selling of food, refreshment or merchandise." (Emphasis supplied.)

Should any doubt remain as to the Congressional intent, it ought to be dispelled by a reading of the Committee Report accompanying H. R. 17 which passed the House in May, 1957 but not the Senate. In the accompanying H. R. 869 it is stated,

> ". . . in the case of the cabaret tax, the 20% rate is particularly onerous because, although this tax is classified as an admissions tax, its base includes not only the price paid for any admissions, but also the amounts paid for refreshments, services, and merchandise. *Moreover, the 20% rate applies only where there is a combination of entertainment and the service of food or beverages.* Where only entertainment is provided the 10% admissions tax usually applies; on the other hand, where there is only the serving of food and beverage, generally no tax is imposed. Thus the 20% tax discriminates against the combination of food and beverages or entertainment, *since either, if provided separately, is taxed at a lesser rate or is not taxed at all.*"[2] (Emphasis supplied.)

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[2]It is interesting to observe that the House, in its Report further noted: "In addition, testimony before a Sub-Committee of your Committee, has indicated that this discriminating high rate of the cabaret tax has had a serious adverse effect on the employment of musicians and other entertainers." (1957 P-H 44,958 Para. 33,005). This observation was undoubtedly based on a study which was reported in Federal Tax Policy for Economic Growth and Stability,

Appellant complains in its Brief that the District Court in refusing to read the Code section literally, concluded that: "A literal translation of the above provision would ascribe to Congressional intent a most arbitrary and unreasonable basis on which the tax is imposed." (App. Br. 18.) As previously pointed out, the Treasury, by its own regulations, has refused to give the words "entitled to be present" a literal meaning. (Rev. Rul. 54-487.)

Appellant in its Brief (p. 19) sets out the issue in these words,

> "Consequently it is our position that it was the intention of Congress to impose a cabaret tax on all amounts paid for food, refreshment, service or merchandise by or for patrons or guests who are entitled to be present during any part of the public performance given at a cabaret for profit."

Joint Committee on the Economic Report published by the United States Government Printing Office, Washington, D. C. It was there stated:

> "A pilot study in five cities, Boston, Detroit, Denver, Minneapolis, and Memphis, was financed by the American Federation of Musicians. On the basis of this study, it was believed by the research agencies that a more extensive survey would support the conclusions:
>
> 1. That establishments subject to this 20 percent cabaret tax are more important sources of employment for musicians, and that job loss in these establishments since 1943 had been much heavier than has been recognized;
>
> 2. That elimination of the 20 percent cabaret tax would lead to a very substantial increase in employment of musicians, entertainers, waiters, waitresses, and other service and kitchen help; and
>
> 3. That loss of tax revenue to the Treasury through elimination of this tax would be offset by increased income-tax payments."

Compare this with the following statement made in the Government Brief filed with this Court in the *Casa de Manana* case (p. 9):

> "It is the Collector's position that taxpayer's establishment was at all times a 'cabaret or other similar place' and that the tax imposed under §1700(e) applied to 'all' refreshments purchased by any patron present during any portion of the entertainment at taxpayer's establishment.
>
> "Section 1700(e) does not require that the consumption of the refreshment be simultaneous with the entertainment but rather contemplates the taxation of any amounts paid throughout the evening by one who is present during the entertainment. This is clear from the use of the language '*all* amounts paid for . . . refreshment.'"

This argument was completely rejected by this Court in the *Casa de Manana* case and the result of the decision was nullification of a Treasury regulation similar to the one invoked in the instant case. There an attempt was made to interpret Section 1700(e) as applying to charges made at the Casa de Manana between 12 midnight and 2:00 a.m. The *Casa de Manana* principle must apply here because the private parties in the Pavillion Room did not constitute a cabaret prior to 10:30 p.m. In other words, what is concededly a private group having a dinner meeting is simply not a cabaret and in attempting to invoke what he considers an applicable ruling, the Commissioner is doing nothing more than what he unsuccessfully attempted to do in the *La Jolla de Manana* case.

So, it is quite obvious that the instant case is but another example of an effort to effect administrative legislation. In at least two recent attempts in this District to

enlarge the operation of Section 1700(e)(1) the Government has met with defeat. An unsuccessful effort to stretch the Code to cover a similar situation is found in *Naylor v. United States,* 102 Fed. Supp. 309. District Judge Ben Harrison was not impressed with Defendant's argument that income from "public" dances held in the private Beverly Hills Club was subject to cabaret tax.

As previously demonstrated, in *La Jolla Casa de Manana v. Riddell,* 106 Fed. Supp. 132 (aff'd, *per cur.,* 206 F. 2d 925) the Government unsuccessfully took a position directly parallel to the one adopted in this case. Despite the fact that the law was made clear in this Circuit in the above 1953 decision as to when a cabaret was a cabaret and when it was not, the Commissioner in 1954 issued a contrary ruling (Rev. Rul. 54-487 C. B. 1954-2, p. 376). Judge Byrne decided that the cabaret tax could not be imposed except during the hours when the establishment was operating as a cabaret. The Commissioner completely ignores this in the above ruling, saying "for the tax to apply, it is not necessary that such patrons or guests be able to witness the entertainment and partake of food or refreshment at the same time."

At this juncture we might point to some of the similarities between the *La Jolla* and *Ciro* cases:

La Jolla Casa de Manana.	*Ciro.*
1. "Some of the patrons to whom refreshment was sold between 12:00 midnight and 2:00 a.m. had been present during part of the entertainment period prior to midnight." (Opin. p. 133.)	1. Some of the patrons in the private parties in the Pavillion Room had been present during part of the entertainment after 10:30 p.m. [R. 72.]

2. "Plaintiff never had, and does not now have, any records showing separately the amount of refreshments sold to each class of patrons." (P. 133.)	2. Plaintiff never had and does not now have any records showing separately the amount of refreshments sold to each class of patrons. [R. 70-71.]
3. The Commissioner proposed an assessment of cabaret tax on all receipts from 12:00 midnight to 2:00 a.m. (P. 133.)	3. The Commissioner assessed cabaret tax receipts prior to entertainment time, 10:30 p.m., as well as during entertainment. [R. 71-72.]
4. After protest by Plaintiff the Commissioner ruled that only one-third of such assessment would be made on the theory that one-third of the receipts represented the portion received from patrons who had been present during some portion of the music and dancing between 9:00 p.m. and 12:00 midnight. (P. 133.)	4. The Commissioner ruled that since 94% of sales in the Main Room were taxable, 94% of sales in the Pavillion Room were taxable on the theory 94% of the patrons in the Pavillion Room private parties stayed to view the entertainment. [R. 71-72.]
5. The Government argued that since the patrons were present at the dancing *before* 12:00 p.m. they could be taxed on sales made after 12:00 p.m. (P. 134.)	5. The Government argues that since Pavillion Room patrons were present during the floor show, sales made *prior* to 10:30 p.m. can be taxed. [R. 49.]

It may be pertinent to note here that the Commissioner of Internal Revenue follows the practice of entering an "acquiesence" or "non-acquiesence" when a decision of the Tax Court of the United States is against him. It is

his practice also to follow or refuse to follow other Court decisions (except those of the Supreme Court of the United States). This procedure is justified on what is asserted to be an interest in the uniform application of the tax laws. In the instant case the Internal Revenue Agents who set up the tax deficiency followed the Commissioner's instructions which are supposed to be uniformly applied in all districts of the United States. The agents neither had the duty to nor apparently did they consider the applicability of certain judicial decisions promulgated in this judicial district and circuit.

Were it not for the rather unique position which the Commissioner of Internal Revenue maintains, the conflict between the decision of this Court in the *Casa de Manana* case and the regulations applied in the case at bar would not be stressed herein. The Tax Court of the United States has in the past, taken the position that it need not follow a Court of Appeals decision in the Circuit in which it is trying a case. But it goes without saying that the District Court for the Southern District of California should follow a decision of the Court of Appeals for the Ninth Circuit whether or not such a decision is contrary to a ruling of the Commissioner of Internal Revenue.

This Court was not in agreement with the Commissioner prior to the *Casa de Manana* decision as to what the following meant:

> "public performance for profit"
>
> "entitled to be present during any portion of such performance"
>
> "where dancing privileges or any other entertainment * * * are afforded the patrons in connection with the serving or selling of food, refreshment or merchandise"
>
> "cabaret"

And, as we have pointed out above, the Commissioner was still in disagreement after the *Casa de Manana* case was decided. In determining what cabaret tax should be imposed on Ciro's he used his own definitions.

Here it might be appropriate to quote from one of the classics.

> "I don't know what you mean by 'glory,'" Alice said. "Humpty Dumpty smiled contemptuously. "Of course you don't—till I tell you. I meant 'there's a nice knock-down argument,'" Alice objected.
>
> "When I use a word," Humpty Dumpty said in rather a scornful tone, "it means just what I choose it to mean—neither more nor less."
>
> "The question is," said Alice, "whether you *can* make words mean so many different things."
>
> "The question is," said Humpty Dumpty, "which is to be master—that's all."
>
> Lewis Carroll's "Through the Looking Glass" Illustrated Editions Company, page 188.

So, even though the Commissioner "*can* make words mean so many different things," the District Court has a right to assume that the Court of Appeals is "master," not the Commissioner.

Attention should be called to a manifest error in Appellant's Brief at page 25. It is stated as follows:

> "Obviously in the La Jolla case, amounts spent from midnight to 2:00 a.m. could not entitle any patron to be present at the dancing or to hear the music which had ceased at midnight and *for that reason* it was held that no tax could be imposed on such. amounts." (Emphasis supplied.)

In the Opinion in the *La Jolla* case (106 Fed. Supp. 132-133) we find the following:

> "On June 28, 1949, the Commissioner of Internal Revenue proposed a deficiency in cabaret tax against plaintiff amounting to $947.10, covering the periods from July to October of 1947, July to September of 1948, and January to April of 1949, based on the total refreshment receipts during such period from midnight to 2:00 o'clock A.M. Plaintiff protested such proposed assessment in writing; thereafter, the Commissioner ruled that only one-third of such proposed deficiency should be assessed against plaintiff, on the theory that approximately one-third of the total receipts represented the portion received from patrons *who had been present during some portion of the music and dancing between 9:00 o'clock P.M. and midnight.* Plaintiff paid the tax and filed a claim for refund, a claim which was rejected. This litigation has resulted." (Italics in original.)

The Court, of necessity, in deciding for the taxpayer determined that the cabaret tax could not be applied on sales to patrons "who had been present during some portion of the music and dancing between 9:00 p.m. and midnight." So, clearly, the reason for the decision in the *La Jolla* case was not that post-midnight patrons were not entitled to be present at the dancing or to hear the music. If the patrons were there, certainly they must have been entitled to be there. In other words, the Court decided in the *La Jolla Casa de Manana* case that the establishment was not a cabaret between 12:00 midnight and 2:00 a.m. therefore sales made during those two hours were not taxable even though the patrons had previously enjoyed the entertainment. In the instant case the Court decided that the private parties in the Pavillion

Room from 7:00 p.m. to 10:30 p.m. were not a cabaret and that sales during these hours were not taxable. It is difficult to see how the District Court could have decided otherwise without being inconsistent with the *Casa de Manana* case.

The Government asserts in its brief that the District Court applied a "subjective test" in arriving at its decision. (App. Br. 23.) Actually, the judge did the same thing that Judge Byrne did in the *Casa de Manana* case. He determined that these private parties did not constitute a cabaret during certain hours (7:00 p.m. to 10:30 p. m.). There is nothing subjective about such a factual determination. Indeed, the judge was careful to limit the applicability of his decision by admonishing:

> "I do not mean to suggest that the Treasury Regulations taxing such receipts should be denied any meaning and effect. Certainly, to allow pre-performance receipts in each and every case to escape the imposition of a tax would serve to provide a facile means for tax avoidance, would compound the already existing difficulties present in tax collection and administration, and would be as much productive of inequities and as lacking in logic as would be the adoption of the other extreme—holding all pre-performance payments by persons remaining for the public performance within the pale of this statute. The only sensible and practical approach to the problem is to *consider the wording of the statute in the light of each factual situation* as it is presented keeping always in mind the objectives and purposes the statute sought to achieve." (Emphasis supplied.) [R. 51-52.]

The Court's holding that the private party activities prior to 10:30 p.m. did not constitute a cabaret is entirely

consistent with the evidence. The public was not admitted and there could not have been a "public performance for profit." It must be conceded that if the entertainers had been brought into the Pavillion Room and the performance had there taken place, the tax would not apply because the mere performance or entertainment does not make what would otherwise be a private performance, a public performance for profit. In making the assessment the Commissioner lost sight of the fact that it is the admittance of the public without restriction that makes for taxability—not that there is entertainment. (*McKenzie v. Maloney,* 71 Fed. Supp. 691; *Daum v. Jarecki,* 123 Fed. Supp. 583; *Southland Club v. Broderick,* 1956 P-H 44,578; *United States v. Lambeth,* 176 F. 2d 810 (C. C. A. 9).)

The interpretation of Section 1700(e) by the District Court is manifestly correct in the light of its legislative history and prior judicial decisions construing it. Accordingly, in reviewing this decision it is suggested that the following rule with respect to tax provisions, enunciated in another tax case, should be applied:

> "It is the established rule not to extend their provisions, by implication, beyond the clear import of the language used, or to enlarge their operations so as to embrace matters not specifically pointed out. In case of doubt they are construed most strongly against the government, and in favor of the citizen." (*Gould v. Gould,* 245 U. S. 151.)

Even assuming, in Appellant's words, that the District Court's test "would be difficult to make and is not a satisfactory one in the exact field of taxation" (App. Br. 23) it is not clear, as indicated in the fn. 2, pp. 10-11, *supra;* whether exclusion of such private parties from cabaret tax would have an over-all adverse tax effect from the Govern-

ment standpoint. In any event, if a change in tax policy is to be made, it is for the Congress to make it.

> " 'If in practice' these sections are causing 'such loss of revenue as to indicate that Congress may have erred in its balancing of the competing considerations involved, the amendment must obviously be enacted by the Congress and not the Commissioner of Internal Revenue or this Court.' " (*Commissioner v. Korell*, 339 U. S. 619, 626 (1950).)

As will be urged in connection with the two remaining issues, herein, the familiar Rule 52(a), F. R. C. P.[3] should control with respect to the trial court's findings of fact regarding the Pavillion Room. The Trial Judge viewed the premises and heard the witnesses. There was, indeed, substantial evidence to support all his findings.

The Ciroette Room.

The Court viewed Ciro's premises in the presence of Counsel for both parties. The Ciroette Room was found to be located on the second floor of Ciro's. The Main (entertainment) Room could be entered by Ciroette private party patrons only after they had descended fourteen steps, cross a breezeway, and passed through two doorways. The Government assessed cabaret tax on 5% of the receipts from private parties held in the Ciroette Room on the ground that 5% of the private party patrons went downstairs to see the floor show after 10:30 p.m. The Trial Court concluded that

> "the nature of these private parties being similar to those conducted in the Pavillion Room my prior

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[3]Rule 52(a) of the Federal Rules of Civil Procedure provides, in part, as follows:

> "Findings of Fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses."

discussion on this subject is pertinent here and does not have to be repeated; however, the reasons for denying the tax on pre-performance receipts in the Pavillion Room are even more potent here in view of the obvious remoteness of the Ciroette Room and the subsequent effort and distance to be traversed for its patrons to observe the floor show. I find therefore, that the tax assessment on the 5% of the Ciroette Room's receipts is improper."

It should be made clear that the assessment of the cabaret tax was on pre-performance receipts from private party patrons in the Ciroette Room. Any purchases in the Main Room after show time by patrons who had come downstairs from the Ciroette Room were taxed at 20% and there is no dispute in this case about the taxability of such post-entertainment charges.

The prior discussion concerning the Pavillion Room, is applicable to the Ciroette private parties and will not be repeated here. It seems appropriate however, to urge that this Court again apply Rule 52(a) (F. R. C. P.) and sustain the Trial Court on the ground that its findings are amply supported by the evidence. Even if this Court should take a different view of the facts it seems evident that there is sufficient evidence in support of the Trial Court's decision so that under Rule 52(a) the decision should be affirmed. As Judge Johnson said in *Nee v. Linwood Securities Co.,* 174 F. 2d 434, 437 (C. A. 8) in sustaining the Trial Court:

"That the trial court could have viewed the facts differently, or that we might perhaps have done so, if we had been the initial trier thereof, does not alone entitle us to reverse. Under Rule 52(a) and its interpretation in the United States Gypsum Co. case, there must exist a stronger basis for over-throwing

a finding of fact than a mere difference in personal judgment. Such evidentiary weight and such convictional certainty must be present that the appellate court does not feel able to escape the view that the trial court has failed to make a sound survey of or to accord the proper effect to all the cogent facts, giving due regard, of course, to the trial court's appraisal of witness credibility where that factor is involved."

Private Parties (Closed House Parties).

On 20 different evenings, usually on Sunday, private organizations held affairs in Ciro's which was then closed to the public. The Government imposed the cabaret tax on the basis of a recent ruling which reads as follows [R. 61]:

> "Where a private organization arranges to hold an affair in a room at a hotel which normally is operated as a cabaret and the affair is held under such circumstances that *the hotel furnishes practically the same services, including entertainment,* during the same hours that the room is operated as a cabaret, *the arrangements made by the private organization are regarded as a mere reservation of tables.* In such case, the Bureau holds that the room is operated as a cabaret on such occasions, even though the patronage is limited to the members, together with the guests of the private organization, and the private organization furnishes entertainment in addition to that furnished by the hotel * * *
>
> "Where a private organization holds a dinner in a room at a hotel, under such circumstances that the hotel does not furnish any entertainment but the private organization does provide dancing facilities for the persons (120) attending by hiring an orchestra,

> or furnishes other entertainment, cabaret tax does not apply to any amount paid in connection with the affair." Special Ruling, August 31, 1949, 5 CCH 1950 Stand. Fed. Tax Rep. Para. 6053. (Emphasis supplied.)

The Ruling has not been passed upon by any Court, however, there are cases dealing with the question of what constitutes a "public performance for profit." (See *United States v. Lambeth,* 176 F. 2d 810 (C. A. 9, 1949); *Naylor v. United States,* 102 Fed. Supp. 309 (S. D. Cal. 1952); *Bomber Club v. Broderick,* U. S. D. C. Kan. 223, 54 Para. 72,685 P-H 1954.)

In reaching out to make this assessment the Commissioner indulged in the fantastic presumption that where a private organization holds an affair in a place which is normally operated as a cabaret, it is subject to cabaret tax on the ground that "the arrangements made by the private organizations are regarded as a mere reservation of tables." This is quite the same as saying that a lessee who rents a furnished apartment obtains from the lessor only a reservation of furniture in the apartment. It should be noted that the Ruling, absurd as it is, applies only "where a private organization arranges to hold an affair in a room at a hotel." Certainly Ciro's is not a room in a hotel.

Not only does the Ruling appear to be invalid but it was improperly applied in this case. Be that as it may, we need not pass on the issue because the District Court found as a fact that "the evidence conclusively establishes that the private organizations themselves contracted for the entertainment and the music." [Opin. R. 62.] The Court was justified in making such a finding on the basis of the testimony. The plaintiff, for example, testified that

in most of the cases the Closed House parties provided their own entertainment and music. Also, they might take only part of the regular Ciro's show and supplement it with their own acts. [R. 201 *et seq.*] As the plaintiff testified, "every party is on its own and we had no control over the show or the party." [R. 206.] Payment was made directly to the entertainers and musicians by the private party. So, by its own terms the ruling cannot apply because Ciro's did not "furnish . . . entertainment."

It is difficult to see how the Court could have decided otherwise. However, even if this Court should interpret the evidence differently, the findings of fact, being supported by substantial evidence, should not be set aside as being "clearly erroneous."

As the Supreme Court said in *United States v. U. S. Gypsum Co.,* 333 U. S. 364, 68 S. Ct. 528

> "Since judicial review of findings of trial courts does not have the statutory or constitutional limitations of findings by administrative agencies or by a jury, this court may reverse findings of fact by a trial court where 'clearly erroneous.' The practice in equity prior to the present Rules of Civil Procedure was that the findings of the trial court, when dependent upon oral testimony where the candor and credibility of the witnesses would best be judged, had great weight with the Appellate Court."

In *United States v. Yellow Cab Company,* 338 U. S. 338, 70 S. Ct. 177 (1949), Mr. Justice Jackson speaking for the Court said:

> "It ought to be unnecessary to say that Rule 52 applies to appeals by the Government as well as to those by other litigants. There is no exception which permits it, even in an antitrust case, to come to this

Court for what virtually amounts to a trial *de novo* on the record of such findings as intent, motive and design. While, of course, it would be our duty to correct clear error, even in findings of fact, the Government has failed to establish any greater grievance here than it might have in any case where the evidence would support a conclusion either way but where the trial court has decided it to weigh more heavily for the defendants. Such a choice between two permissible views of the weight of evidence is not 'clearly erroneous.' "

Judge Sanborn of the Court of Appeals for the Eighth Circuit, said in *Cleo Syrup Corp. v. Coca-Cola Co.,* 139 F. 2d 416:

"This Court, upon review, will not retry issues of fact or substitute its judgment with respect to such issues for that of the trial court. (citing cases) The power of a trial court to decide doubtful issues of fact is not limited to deciding them correctly. (citing cases) In a non-jury case, this Court may not set aside a finding of fact of a trial court unless there is no substantial evidence to sustain it, unless it is against the clear weight of the evidence, or unless it was induced by an erroneous view of the law." (Citing cases.)

The Supreme Court in *McCaughn v. Real Estate Land Title and Trust Co.,* 297 U. S. 606, reversed a decision of the Court of Appeals which had reversed a judgment of the District Court, rendered in a tax case prior to the adoption of Rule 52. There the District Court trying the case without a jury held that a certain transfer had been made in contemplation of death. The Court of Appeals on review, decided that the transfer was not made in con-

templation of death and reversed the judgment. In reversing the Court of Appeals, the Supreme Court said:

> "the instant case is controlled by the established rules relating to appellate review in actions at law where a jury trial has been waived . . . where a general verdict is found by the trial court, it has the same effect as the verdict of a jury. The Appellate Court cannot pass upon the weight of evidence (citations)" . . . "The ultimate question for the decision of the trial court was one of fact and its general verdict was conclusive. The Circuit Court of Appeals was without authority to weigh the evidence and to make its own findings."

Rule 52(a) and the general rule as enunciated by the Supreme Court was followed by this Court in a recent tax case (*United States v. Lambeth,* 176 F. 2d 810) involving the identical section here under consideration. *i. e.* Section 1700(e). This Court through Judge Bone there remarked:

> "On this record we think that the case falls within Rule 52(a) of the Federal Rules of Civil Procedure, 28 U. S. C. A., in part providing: 'Findings of fact shall not be set aside unless clearly erroneous, * * *.' Clear error calling for reversal is not present and the Government's presentation fails to convince us otherwise. Affirmed." (*Wittmayer v. United States* (9 Cir. 1941), 118 F. 2d 808, 811.)

In the *Lambeth* case the taxpayer claimed to be operating a private club; however, taxpayer did not have a club license under Oregon law. In fact taxpayer's license "contemplated services to the general public." This Court in its opinion noted that " 'admittance' cards were apparently accessible to anyone who decided to 'join'." Never-

theless, even with such a "liberal guest policy" it was held that the taxpayer was not "serving the public and was thus not furnishing a public performance for profit within the definition of the Federal taxing statute." (See also *McKenzie v. Maloney,* 71 Fed. Supp. 691; and *Southland Club v. Broderick,* 1956 P-H 44,578; *cf. Sir Francis Drake v. United States,* 75 Fed. Supp. 668 (N. D. Cal.), decided on a 1941 assessment.)

Despite the decision of this Court in the *Lambeth* case the Commissioner maintains that a private party held at Ciro's when it was closed to the public constitutes "a public performance for profit."

Certainly, the findings of fact of the trial judge adverse to the Commissioner on this issue are not "clearly erroneous."

Conclusion.

For the foregoing reasons the decision appealed from should be affirmed.

Respectfully submitted,

Ernest R. Mortenson,

Attorney for Appellee.

No. 16107

United States Court of Appeals

for the Ninth Circuit

RICHARD C. HOY, District Director of Immigration and Naturalization Service, Los Angeles, California, Appellant,

vs.

MANUEL MENDOZA-RIVERA, Appellee.

Transcript of Record

Appeal from the United States District Court for the Southern District of California, Central Division

FILED
OCT - 9 1958
PAUL P. O'BRIEN, CLERK

Phillips & Van Orden Co., Fourth and Berry Sts., San Francisco, Calif.—10-7-58

No. 16107

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Los Angeles 14, California. [1]*

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* Page numbers appearing at bottom of page of Original Transcript of Record.

In the United States District Court, Southern District of California, Central Division

No. 813-57 HW

MANUEL MENDOZA-RIVERA, Plaintiff,

vs.

ALBERT DEL GUERCIO, as District Director of the Immigration and Naturalization Service, Los Angeles, California, Defendant.

PETITION FOR JUDICIAL REVIEW OF ORDER OF DEPORTATION AND DECLARATORY JUDGMENT

Plaintiff alleges:

I.

This petition is filed and these proceedings are instituted against the defendant pursuant to Title 28, U.S.C.A. Section 2201, commonly known as the Declaratory Judgment Act, and Title 5, U.S.C.A. Section 1009, commonly known as Section 10 of the Administrative Procedure Act, for a judgment declaring that plaintiff is not deportable from the United States as charged by the defendant.

II.

That the plaintiff is a resident of the County of Los Angeles, State of California, within the jurisdiction of this Court.

III.

That the defendant, Albert Del Guercio, is the District Director of the Immigration and Natural-

ization Service, Department of Justice, in Los Angeles, California. [2]

IV.

That the plaintiff is a native and citizen of Mexico, 24 years of age, who last entered the United States at San Ysidro, California, on or about March 15, 1955.

V.

That plaintiff on or about January 10, 1952, at the age of 18, was convicted under Section 11500, Health and Safety Code of the State of California, of possession of flowering tops and leaves of Indian Hemp, committed on October 25, 1951. He was sentenced to ninety days in the Los Angeles County Jail, which, under California law, made the offense for which he was convicted a misdemeanor.

VI.

That Indian Hemp is commonly known as Marihuana.

VII.

That on or about January 11, 1957, the plaintiff was ordered deported from the United States as an alien who was excludable at the time of entry into the United States because of previously having been convicted of illicit possession of a narcotic drug in violation of Section 11500, Health and Safety Code of California, by a Special Inquiry Officer, of the Immigration and Naturalization Service at Los Angeles, California.

VIII.

That on or about January 31, 1957, the Board of

Immigration Appeals, United States Department of Justice, ordered the proceedings terminated on the ground that at the time of his last entry in March 1955, a record of conviction of the mere possession of a narcotic drug was not a ground of excludability.

IX.

That on or about April 12, 1957, the plaintiff was ordered deported from the United States, by a Special Inquiry Officer, of the Immigration and Naturalization Service, acting as a subordinate and under the direction of the defendant, on the charge stated in the Order To Show Cause:

> "Section 241 (a)(11) of the Immigration and Nationality Act, in that, you at any time have been convicted of a violation of any law or regulation relating to the illicit possession of narcotic drugs: Section 11500, Health and Safety Code of the State of California." [3]

X.

That on or about May 20, 1957, the Board of Immigration Appeals, United States Department of Justice, Washington, D. C., affirmed the aforementioned decision of the Special Inquiry Officer and ordered that the Appeal of the plaintiff to said Board be dismissed.

XI.

That on or about June 6, 1957, the defendant, acting as the aforesaid, and through a subordinate, advised that the plaintiff was granted to July 15, 1957,

to depart from the United States under the outstanding Order of Deportation. It is the intention of the defendant to take the plaintiff into custody and deport him from the United States under the Order of Deportation if he has not departed under the Order by July 15, 1957.

XII.

That defendant has made an error in law in that the charge upon which the Order of Deportation is based is not applicable.

Section 241 (a)(11) of the Immigration and Nationality Act, as amended by the Act of July 18, 1956, does provide for the deportation of an alien who at any time has been convicted of a violation of any law or regulation relating to the illicit possession of narcotic drugs. However, the Act of July 18, 1956, commonly known as the Narcotic Control Act of 1956, makes a clear distinction between the terms narcotic drugs and marihuana. In its subtitle it states that its purpose is "to provide for a more effective control of narcotic drugs and marihuana, * * *". The second part of Subsection 11 of Section 241 (a)(11) of the Immigration and Nationality Act, as amended by the Narcotic Control Act of 1956, does not use the term narcotic drugs, but relates to the possession of marihuana and other specifically named substances for certain specific purposes, but does not provide for deportation for the conviction of the mere possession of marihuana. The legislative history and the committee reports pertaining to the Narcotic Control Act of 1956 also

show that a definite distinction is made between the terms narcotic drugs and marihuana. [4]

Title 21, U.S.C.A. 171, relating to Food and Drugs, in defining the term narcotic drug states that it shall have the meaning ascribed to the term narcotic drug by Section 3228 (g) of Title 26. This section pertains to the 1939 Code and is presently found in Title 26, U.S.C.A. Section 4731 (1954 Code), and marihuana is not included in the definition. Title 21, U.S.C.A. 176 does define marihuana, but not as a narcotic or a narcotic drug. Plaintiff was convicted of the mere possession of marihuana and since marihuana does not come within the definition of a narcotic drug, the charge on which the Order of Deportation is based does not apply in the case of this plaintiff.

XIII.

Plaintiff has exhausted his administrative remedies.

Wherefore, the plaintiff prays that the Court review the record of his deportation proceedings and enter judgment that he is not deportable from the United States upon the charge contained in the Order of Deportation, and that preceding the judgment of the Court, defendant and his subordinates be restrained from taking plaintiff into custody and effecting his deportation from the United States.

Dated: July 3, 1957.

/s/ HARLIN M. FULLER,
Attorney for Plaintiff. [5]

[Endorsed]: Filed July 3, 1957.

[Title of District Court and Cause.]

ANSWER TO PETITION FOR JUDICIAL REVIEW

The defendant above named, by and through the undersigned, in Answer to the Petition for Judicial Review on file herein, Admits, Denies and Alleges as follows:

I.

Neither admits nor denies the allegations contained in Paragraph I of plaintiff's Petition, and same being a conclusion of law.

II.

In answer to Paragraph II of plaintiff's Petition, defendant does not have sufficient information upon which to base a belief as to the truth of the allegations therein contained and on that ground denies generally and specifically each and every allegation therein. [6]

III.

Admits the allegations contained in Paragraphs III, IV, V and VI of plaintiff's Petition.

IV.

Answering Paragraph VII of plaintiff's Petition, defendant denies that on or about January 11, 1957, the plaintiff was ordered deported, and alleges that on or about January 3, 1957, the plaintiff was ordered deported. Except as denied all other allegations contained in Paragraph VII are admitted.

V.

Answering Paragraph VIII of plaintiff's Petition, defendant admits the allegations contained therein.

VI.

Answering Paragraph IX of plaintiff's Petition, defendant admits all of the allegations contained in said Paragraph IX with the exception of the phrase "acting as a subordinate and under the direction of the defendant" which allegation the defendant denies.

VII.

Answering Paragraph X of plaintiff's Petition, defendant admits the allegations contained therein.

VIII.

Answering Paragraph XI of plaintiff's Petition, defendant denies that it is the intention of the defendant to take the plaintiff into custody and deport him from the United States under the Order of Deportation if he has not departed under the Order by July 15, 1957. The Immigration and Naturalization Service will not remove the plaintiff from the jurisdiction of this court during the pendency of the present litigation. Except as denied all other allegations contained in Paragraph XI of plaintiff's Petition are admitted. [7]

IX.

Answering Paragraph XII of plaintiff's Petition, defendant denies generally and specifically each and every allegation contained therein.

X.

Answering Paragraph XIII of plaintiff's Petition, defendant admits the same.

For a Further, Separate and First Affirmative Defense, Defendant Alleges:

I.

That the plaintiff has been accorded a full and fair hearing in conformity with law to determine his right to be and remain in the United States. There will be offered in evidence when this cause is tried a certified record of the Immigration and Naturalization Service, Department of Justice, relating to the plaintiff, containing the complete record of the deportation proceedings before the Immigration and Naturalization Service.

For a Further, Separate and Second Affirmative Defense, Defendant Alleges:

I.

Plaintiff's Petition on file herein fails to state a claim upon which relief can be granted.

Wherefore, defendant prays for a judgment dismissing the said Petition, denying the relief prayed for therein, and for such other relief as to the Court seems just and proper in the [8] premises.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,

NORMAN R. ATKINS,
Assistant U. S. Attorney,
/s/ NORMAN R. ATKINS,
Assistant U. S. Attorney,
Attorneys for Defendant. [9]

Affidavit of Service by Mail Attached. [10]

[Endorsed]: Filed August 9, 1957.

[Title of District Court and Cause.]

PRE-TRIAL CONFERENCE ORDER

Following pre-trial proceedings pursuant to Rule 16 of the Federal Rules of Civil Procedure and Local Rule 9 of this Court It Is Ordered:

I.

This is an action for judicial review of deportation proceedings based on a complaint filed by plaintiff Manuel Mendoza-Rivera, against Albert Del Guercio, as District Director of the Immigration and Naturalization Service, Los Angeles, California, defendant. The defendant has answered.

II.

Federal jurisdiction is involved upon the ground that the complaint was filed and these proceedings were instituted against the defendant pursuant to Title 28, U.S.C.A., Section 2201 and Title 5, U.S.C.A., Section 1009, for a judgment declaring that plaintiff is not deportable from the United States on the charge in the Order to Show Cause and the Warrant of Deportation. [11]

III.

The following facts are admitted and require no proof:

(A) Plaintiff Manuel Mendoza-Rivera is a native and citizen of Mexico, 24 years of age;

(B) Plaintiff last entered the United States at San Ysidro, California on or about March 15, 1955;

(C) Plaintiff was convicted in the Superior Court of the State of California, at Los Angeles, California, on January 10, 1952 for violation of 11,500, Health and Safety Code of the State of California, possession of flowering tops and leaves of Indian Hemp, committed on October 25, 1951.

(D) Indian Hemp is known as marihuana.

(E) A deportation hearing was accorded plaintiff and following completion of said hearing on April 12, 1957 the Special Inquiry Officer of the Immigration and Naturalization Service made the following order:

> "Order: It is ordered that the Respondent be deported from the United States in the manner provided by law on the charge contained in the Order to Show Cause."

The charge as stated in the Order To Show Cause reads as follows:

> "Section 241(a)(11) of the Immigration and Nationality Act, in that, you at any time have been convicted of a violation of any law or regulation relating to the illicit possession of narcotic drugs; Section 11500, Health and Safety Code of the State of California."

(F) On May 20, 1957 the Board of Immigration Appeals, Washington, D. C. made the following order:

> "Order: It is ordered that the appeal be and the same is hereby denied."

IV.

There are no reservations as to facts recited in Paragraph III above.

V.

There are no facts in issue which have not been admitted above and there are no facts remaining to be litigated at the trial. [12]

VI.

The exhibits to be offered at the trial, together with a statement of all admissions by and all issues between the parties with respect thereto are as follows:

(A) The defendant will present at the time of trial the certified file of the Immigration and Naturalization Service relating to the deportation proceedings of the plaintiff herein.

VII.

The following issues of law, and no others, remain to be litigated upon the trial:

(A) Does Section 241(a)(11) of the Immigration and Nationality Act as amended by the Narcotic Control Act of 1956, make a distinction between a narcotic drug and marihuana whereby a convic-

tion of possession of marihuana would not be construed as a conviction of possession of a narcotic drug?

(B) Does Section 241(a)(11) as amended by the Narcotic Control Act of 1956, require that an alien who has been convicted of the mere possession of marihuana be deported from the United States?

(C) Do Sections 11,001 to 11,500 of the Health and Safety Code of the State of California define narcotic drugs to include marihuana, and if so shall this definition or the definition and meaning of the term "narcotic drug" as set out in the Federal statutes govern the determination as to whether an alien has been convicted of the possession of a narcotic drug as that term is used in Section 241 (a) (11) of the Immigration and Nationality Act as amended by the Narcotic Control Act of 1956?

Dated: November 4, 1957.

/s/ HARRY C. WESTOVER,
United States District Judge.

Approved as to form and substance:

/s/ HARLIN M. FULLER,
Attorney for Plaintiff.

/s/ NORMAN R. ATKINS,
Attorney for Defendant. [13]

[Endorsed]: Filed November 4, 1957.

[Title of District Court and Cause.]

OPINION

Plaintiff, Manuel Mendoza-Rivera, is a citizen of Mexico who has been in the United States since the age of two years. On January 10, 1952, in the Superior Court of the State of California, in and for the County of Los Angeles, he was convicted of possession of flowering tops and leaves of Indian Hemp, in violation of Section 11,500 of the Health and Safety Code of the State of California, and was sentenced to imprisonment for the term of ninety days.

On December 20, 1956, some five years later, plaintiff herein was served with an Order to Show Cause and a Notice of Hearing, which set out that inasmuch as plaintiff [16] was convicted on January 10, 1952, at Los Angeles, California, of the offense of possession of flowering tops and leaves of Indian Hemp (marihuana), he was subject to be taken into custody and deported, pursuant to the provisions of Section 241(a) (11) of the Immigration and Nationality Act. A Hearing was had before a special inquiry officer on January 3, 1957, and the plaintiff was ordered deported. From this Order plaintiff appealed, and on January 31, 1957, the Chairman of the Board of Immigration Appeals made an order in which he reviewed the action taken by the hearing officer. The Order reads in part as follows:

"* * * at the time of his [plaintiff's] last entry

on March 15, 1955 the respondent was not excludable by the law then existing since mere naked possession of a narcotic was not a ground of excludability * * *. Mere possession was not made a ground of inadmissibility until the amendment to the Immigration and Nationality Act by Section 301(a), Act of July 18, 1956 (70 Stat. 575). Since the alien had entered the United States prior to the date of the amendment he was not at the time of entry within one of the classes of aliens excludable by the law existing at the time of such entry. Accordingly, we find the charge stated in the Order to Show Cause not sustained. The proceedings will be terminated."

However, on March 11, 1957, the Immigration and Naturalization Service sent to plaintiff herein a second Order to Show Cause and Notice of Hearing, alleging in substance the charges as made in the Order to Show Cause dated December 20, 1956. A hearing was had upon the Order to Show [17] Cause, and on April 12, 1957, the special inquiry officer held again that the plaintiff herein be deported.

An appeal was taken by this plaintiff to the Board of Immigration Appeals, Department of Justice, Washington, D. C., and on May 20, 1957, the Chairman of the Board of Appeals filed an Order holding that plaintiff was deportable under Section 241(a) (11) of the Immigration and Nationality Act, as amended by the Act of July 18, 1956, and dismissed the appeal. Thereafter this petition for judicial review of the Order of Deportation was filed by the plaintiff.

On July 18, 1956 Congress amended the Immigration and Nationality Act and provided mere possession of a narcotic drug would be sufficient to justify deportation. Section 1251, Title 8, Subdivision (a) (11) provides that an alien may be deported:

"* * * who at any time has been convicted of a violation of any law or regulation relating to the illicit traffic in narcotic drugs, or who has been convicted of a violation of any law or regulation governing or controlling the taxing, manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation, exportation, or the possession for the purpose of the manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation or exportation of opium, coca leaves, heroin, marihuana, any salt derivative or preparation of opium or coca leaves or isonipecaine or any addiction-forming or addiction-sustaining opiate; * * *" [18]

The sole contention before the Court in this proceeding is whether the term "narcotic drug" in Section 1251 (a) (11) includes marihuana.

Examination of Section 1251 (a) (11) indicates that Congress has seen fit to include in the section a number of different offenses. The section provides that an alien may be deported (1) who has at any time been convicted of a violation of any law or regulation relating to the illicit traffic in narcotic drugs; (2) who has been convicted of a violation of any law or regulation governing or

controlling the taxing, manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation, exportation, or (3) the possession for the purpose of the manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation or exportation of opium, coca leaves, heroin, marihuana, any salt derivative or preparation of opium or coca leaves or isonipecaine or any addiction-forming or addiction-sustaining opiate.

In Item (3) above, Congress uses the term "marihuana, * * * or any addiction-forming or addiction-sustaining opiate." If Congress wished to include within the definition of narcotic drugs in (1) above "marihuana", so there would have been no question as to its intent, it could very easily have added the word "marihuana." Congress knew, or should have known, that there had been a question as to whether the term "narcotic drugs" included marihuana. Certainly it should have been cognizant of the implications which would arise in omitting the term "marihuana."

If plaintiff herein is to be deported, he must be deported because he has been convicted of a violation [19] relating to illicit traffic in narcotic drugs. Plaintiff admits that marihuana under the laws of the State of California is classified as a narcotic drug but contends marihuana is not included in the term "narcotic drugs" as defined by Section 1251 (a) (11).

Section 101 of the Narcotic Control Act of 1956

covers unlawful acquisition of marihuana. Section 102 treats of transportation of marihuana. These sections refer to the amendments of the 1954 Code —"The Narcotic Drug Import and Export Act." Section 103, which amends Section 7237 of the Internal Revenue Code states: "Violation of narcotic drug and marihuana laws."

Section 105 relates to the importation of narcotic drugs. Section 106 refers to the smuggling of marihuana. Section 108 deals with unlawful possession of narcotic drugs and marihuana on vessels.

It would appear that Congress, in enacting Public Law 728, kept in mind a distinction between marihuana and narcotic drugs. In many of the sections as noted above Congress referred to narcotic drugs and marihuana, and Section 106 refers exclusively to the smuggling of marihuana. The amendment to the Immigration and Nationality Act with which we are concerned in this proceeding was a part of Public Law 728. We are at a loss to comprehend how Congress could make a distinction between narcotic drugs and marihuana in the first part of Public Law 728 and not make the same distinction in the last part.

A review of Public Law 728 forces us to conclude that Congress distinguishes between "narcotic drugs" and "marihuana." The section under which the government seeks to deport plaintiff used only the term "narcotic drugs." [20] We must hold that Congress did not intend to include marihuana within the definition of narcotic drugs.

The Court will find plaintiff not deportable upon the grounds as set forth in the Order of Deportation. Counsel for plaintiff will prepare Findings of Fact and Judgment in conformity with the rule.

Dated this 24th day of Feb., 1958.

/s/ HARRY C. WESTOVER,
U. S. District Judge. [21]

[Endorsed]: Filed February 24, 1958.

United States District Court, Southern District of California, Central Division

No. 813-57 HW

MANUEL MENDOZA-RIVERA, Plaintiff,

vs.

RICHARD C. HOY, as District Director of the Immigration and Naturalization Service, Los Angeles, California, Defendant.

FINDINGS OF FACT, CONCLUSIONS OF LAW AND JUDGMENT

This cause came on regularly for trial on January 13, 1958, and thereafter was continued to and concluded on February 24, 1958 in the above-entitled Court, before the Honorable Harry C. Westover, Judge Presiding, sitting without a jury. Plaintiff's petition was filed and the proceedings were instituted against the defendant pursuant to

Title 28, U.S.C.A., Section 2201, commonly known as the Declaratory Judgment Act, and Title 5, U.S.C.A. Section 1009, commonly known as Section 10 of the Administrative Procedure Act, for a judgment declaring that plaintiff is not deportable from the United States as charged by the defendant. Defendant filed an Answer to said Petition for judicial review. A pre-trial conference was had and a pre-trial order was made wherein it was stated that there were no facts in issue which have not been admitted as set forth in the pre-trial conference order, and that there were no facts remaining to be litigated at the trial. The only [24] issue remaining for determination was whether the term "narcotic drug", in Section 241(a)(11) of the Immigration and Nationality Act of 1952, as amended by Public Law 728, passed July 18, 1956 [8 U.S.C.A. 1251(a)(11)] includes marihuana. At the commencement of the trial it was stipulated and agreed to by counsel and ordered that the proceedings be and they were amended to insert the name of Richard C. Hoy, the present District Director of the Immigration and Naturalization Service, in lieu and in place of Albert Del Guercio, who was District Director of the Immigration and Naturalization Service at Los Angeles, California, at the commencement of these proceedings, as defendant. At the trial all parties were afforded full opportunity to be heard and to argue the law. The Court has fully considered the Petition, Answer, arguments and memoranda of counsel. Upon the entire record, the Court makes the following:

Findings of Fact

I.

Plaintiff is an alien, a native and citizen of Mexico, twenty-five years of age, who first came to the United States at the age of two years, and who last entered the United States at San Ysidro, California, on or about March 15, 1955.

II.

Richard C. Hoy is the present District Director of the Immigration and Naturalization Service, Department of Justice, at Los Angeles, California.

III.

On January 10, 1952, in the Superior Court of the State of California, in and for the County of Los Angeles, the Plaintiff was convicted of possession of flowering tops and leaves of Indian Hemp, in violation of Section 11,500 Health and Safety Code of the State of California. For this offense he was sentenced to 90 days in the Los Angeles County Jail. Indian Hemp is commonly known as Marihuana.

IV.

On March 11, 1957, the acting District Director of the Immigration [25] and Naturalization Service at Los Angeles, California, sent to the plaintiff herein an Order to Show Cause and Notice of Hearing, which set out that in as much as Plaintiff was convicted on January 10, 1952, at Los Angeles, California, for the offense of possession of flowering tops and leaves of Indian Hemp, committed on

October 25, 1951, he was subject to be taken into custody and deported, pursuant to Section 241(a)(11) of the Immigration and Nationality Act, in that he had been convicted of a law relating to the illicit possession of narcotic drugs, Section 11,500, Health and Safety Code of the State of California. A hearing was had upon the Order to Show Cause, and on April 12, 1957, the Special Inquiry Officer held that Plaintiff herein be deported. An appeal was taken by this plaintiff to the Board of Immigration Appeals, Department of Justice, Washington, D. C., and on May 20, 1957, the chairman of the Board of Immigration Appeals filed an Order holding that plaintiff was deportable under Section 241(a)(11) of the Immigration and Nationality Act, as amended by the Act of July 18, 1956, and dismissed the appeal. Thereafter, this Petition for judicial review of the Order of Deportation was filed by the Plaintiff.

V.

On July 18, 1956, Congress passed Public Law 728, also known as the Narcotic Control Act of 1956, and therein amended Section 241(a)(11) of the Immigration and Nationality Act of 1952, by providing that a conviction for the mere possession of a narcotic drug would be sufficient to justify deportation.

Section 241(a)(11) of the Immigration and Nationality Act of 1952 prior to the amendment enacted July 18, 1956 provided that an alien may be deported:

"(who) is, or hereafter at any time after entry has been, a narcotic drug addict, or who at any time has been convicted of a violation of any law or regulation relating to the illicit traffic in narcotic drugs, or who has been convicted of a violation of any law or regulation governing or controlling the taxing, manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation, exportation, or the possession for [26] the purpose of the manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation or exportation of opium, coca leaves, heroin, marihuana, any salt derivative or preparation of opium or coca leaves or isonipecaine or any addiction-forming or addiction sustaining opiate; * * *"

Section 241(a)(11) of the Immigration and Nationality Act as amended July 18, 1956, Title 8, U.S.C.A. 1251 (a)(11) provides that an alien may be deported:

"(who) is, or hereafter at any time after entry has been, a narcotic drug addict, or who at any time has been convicted of a violation of, or a conspiracy to violate, any law or regulation relating to the illicit possession of or traffic in narcotic drugs, or who has been convicted of a violation of, or a conspiracy to violate, any law or regulation governing or controlling the taxing, manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation, exportation, or the possession for the purpose of the manufacture,

production, compounding, transportation, sale, exchange, dispensing, giving away, importation, or exportation of opium, coca leaves, heroin, marihuana, any salt derivative or preparation of opium or coca leaves or isonipecaine or any addiction-forming or addiction-sustaining opiate; * * *"

VI.

House Report No. 2388, dated June 19, 1956, and Conference Report No. 2546, dated June 29, 1956 on Public Law 728 which was thereafter passed by Congress on July 18, 1956, which amended Section 241(a)(11) of the Immigration and Nationality Act of 1952, distinguished between the narcotic and marihuana possessor and also distinguished between marihuana and narcotic drugs in other ways.

Public Law 728, entitled "Narcotic Control Act of 1956" has the following sub-title: "Act To Amend The Internal Revenue Code of 1954 And The Narcotic Drug Import And Export Act To Provide For a More [27] Effective Control Of Narcotic Drugs And Marihuana, And For Other Related Purposes." Section 101 of the Act pertains to unlawful acquisition of marihuana; Section 102 of the Act pertains to the unlawful transportation of marihuana; Section 103 of the Act relates to both narcotic drugs and marihuana; Section 105 pertains to the Importation of Narcotic Drugs; Section 106 pertains to smuggling of marihuana; Section 108 pertains to the "unlawful

possession of narcotic drugs and marihuana on vessels." There is no language or expression in Public Law 728 or in the Congressional Committee Reports on this statute which indicate or express the intention that marihuana was included in the term "narcotic drugs" as that term is used in Section 241(a)(11) of the Immigration and Nationality Act of 1952, as amended by the said statute.

Conclusions of Law

In consideration of the foregoing Findings of Fact, it is concluded:

I.

This Court has jurisdiction over this proceeding by authority of Title 28, U.S.C.A. Section 2201 and Title 5, U.S.C.A. Section 1009.

II.

Marihuana is not a narcotic drug within the meaning of Section 241(a)(11) of the Immigration and Nationality Act of 1952 as amended by Public Law 728, passed July 18, 1956 [8 U.S.C.A. 1251(a)(11)].

III.

Plaintiff is not subject to deportation under Section 241(a)(11) of the Immigration and Nationality Act of 1952 as amended by Public Law 728, passed by Congress July 18, 1956 [8 U.S.C.A. 1251(a)(11)].

IV.

The Order of Deportation of the Immigration and Naturalization Service, Department of Justice,

directing the deportation of the plaintiff Manuel Mendoza-Rivera is unlawful and is void in that it is in excess of the statutory authority.

Judgment

In accordance with the foregoing Findings of Fact and Conclusions [28] of Law, it is Ordered, Adjudged and Decreed:

The Order of Deportation of the Immigration and Naturalization Service, Department of Justice, directing the deportation of the plaintiff Manuel Mendoza-Rivera is hereby set aside and declared null and void and of no effect.

Dated this 10th day of March, 1958.

/s/ HARRY C. WESTOVER,
U. S. District Judge. [29]

Acknowledgment of Service Attached. [30]

[Endorsed]: Filed March 10, 1958. Entered March 12, 1958.

[Title of District Court and Cause.]

STIPULATION SUBSTITUTING RICHARD C. HOY AS DEFENDANT AND ORDER THEREON

It Is Hereby Stipulated by and between the parties hereto, through their respective attorneys of record, that Richard C. Hoy, District Director of Immigration and Naturalization at Los Angeles, California, who took office and was officially appointed on January 6, 1958, be substituted as defendant in the above entitled action in the place and stead of Albert Del Guercio.

Dated: This 3rd day of July, 1958.

/s/ HARLIN M. FULLER,
Attorney for Plaintiff.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief, Civil Division,
/s/ NORMAN R. ATKINS,
Assistant U. S. Attorney,
Attorneys for Defendant.

It Is So Ordered this 8th day of July, 1958.

/s/ HARRY C. WESTOVER,
U. S. District Judge. [31]

[Endorsed]: Filed July 9, 1958.

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice Is Hereby Given that Richard C. Hoy, District Director of the Immigration and Naturalization Service at Los Angeles, California, defendant above named, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the final judgment entered in this action on March 12, 1958.

Dated: April 24, 1958.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,
NORMAN R. ATKINS,
Assistant U. S. Attorney,
/s/ NORMAN R. ATKINS,
Attorneys for Defendant. [32]

Affidavit of Service by Mail Attached. [33]

[Endorsed]: Filed April 24, 1958.

[Title of District Court and Cause.]

APPLICATION FOR EXTENSION OF TIME IN THE FILING AND DOCKETING OF THE RECORD ON APPEAL AND ORDER THEREON; AFFIDAVIT OF NORMAN R. ATKINS [34]

The defendant herein herewith respectfully applies for an extension of time to and including July 23, 1958, in which to file and docket the record on appeal in the within case. The reasons for the application of the within extension are contained in the Affidavit of Norman R. Atkins, attached hereto.

Dated: May 28, 1958.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,
NORMAN R. ATKINS,
Assistant U. S. Attorney,
/s/ NORMAN R. ATKINS,
Attorneys for Defendant.

It Is So Ordered this 28th day of May, 1958.

/s/ LEON R. YANKWICH,
U. S. District Judge. [35]

Affidavit of Norman R. Atkins

State of California,
County of Los Angeles—ss.

Norman R. Atkins, being first duly sworn, deposes and says:

That he is an Assistant United States Attorney for the Southern District of California and one of the attorneys of record in the within action;

That because of time consumed in consulting with and obtaining authorization from the appropriate government officials concerning the within action, insufficient time remains in which to consider, prepare and docket the record on appeal.

/s/ NORMAN R. ATKINS,
Affiant.

Subscribed and sworn to before me this 28th day of May, 1958.
[Seal] /s/ LOIS M. PARKINSON,
Notary Public in and for said County and State.
My Commission Expires Feb. 24, 1961. [36]

Affidavit of Service by Mail Attached. [37]

[Endorsed]: Filed May 28, 1958.

[Title of District Court and Cause.]

CERTIFICATE BY CLERK

I, John A. Childress, Clerk of the above-entitled Court, hereby certify that the items listed below constitute the transcript of record on appeal to the United States Court of Appeals for the Ninth

Circuit, in the above-entitled matter:

A. The foregoing pages numbered 1 to 39, inclusive, containing the original:

Petition for Judicial Review.

Answer.

Pre-Trial Conference Order.

Minute Order 11/4/57 re pretrial conference.

Minute Order 1/13/58 re trial.

Opinion.

Minute Order 2/24/58 re further trial.

(copy) Clerk's notice of entry of judgment.

Findings of Fact, Conclusions of Law and Judgment.

Stipulation substituting party defendant.

Notice of Appeal.

Application for extension of time to file and docket record on appeal, etc.

Designation of Record on Appeal.

B. Defendant's Exhibit "A".

I further certify that my fee for preparing the foregoing record, amounting to 1.60, has not been paid by appellant.

Dated: July 21, 1958.

[Seal] JOHN A. CHILDRESS,
Clerk,
/s/ By WM. A. WHITE,
Deputy Clerk.

[Endorsed]: No. 16107. United States Court of Appeals for the Ninth Circuit. Richard C. Hoy, District Director of Immigration and Naturalization Service, Los Angeles, California, Appellant, vs. Manuel Mendoza-Rivera, Appellee. Transcript of Record. Appeal from the United States District Court for the Southern District of California, Central Division.

Filed and Docketed: July 22, 1958.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

United States Court of Appeals
For The Ninth Circuit

No. 16107

RICHARD C. HOY, District Director Immigration and Naturalization Service, etc.,
Appellant,

vs.

MANUEL MENDOZA-RIVERA, Appellee.

APPELLANT'S STATEMENT OF POINTS ON APPEAL

The appellant hereby designates the following Points on Appeal in the above entitled matter:

I.

Conviction of an alien under California Law of

the offense of unlawful possession of marihuana is a conviction of "illicit possession of * * * narcotic drugs" within the meaning of the 1956 Amendment to Section 241(a)(11) of the Immigration and Nationality Act of 1952 [8 U.S.C. §1241(a)(11), Supp. 5, 1958] and therefore constitutes a proper ground for deportation of said alien.

Dated: July 31, 1958.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,
NORMAN R. ATKINS,
Assistant U. S. Attorney,
/s/ NORMAN R. ATKINS,
Attorneys for Appellant.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed August 2, 1958. Paul P. O'Brien, Clerk.

[Title of Court of Appeals and Cause.]

APPELLANT'S DESIGNATION OF RECORD TO BE PRINTED

Appellant hereby designates the following record to be printed in the above-entitled matter.

1. Petition for Judicial Review;
2. Answer;
3. Pre-trial Conference Order;
4. Opinion;

5. Findings of Fact, Conclusions of Law and Judgment;

6. Stipulation substituting party defendant;

7. Notice of Appeal;

8. Application for extension of time to file and docket record on appeal, etc.;

9. Designation of Record on Appeal;

10. Stipulation regarding Exhibit A;

11. Appellant's Designation of Record to be Printed;

12. Appellant's Statement of Points on Appeal.

Counsel for the parties have stipulated, subject to the approval of the Court, that Exhibit A received in evidence, which consists of the Administrative Record of the Immigration and Naturalization Service, might be considered in its original form and need not be printed.

Dated: July 31, 1958.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,
NORMAN R. ATKINS,
Assistant U. S. Attorney,
/s/ NORMAN R. ATKINS,
Attorneys for Appellant.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed August 2, 1958. Paul P. O'Brien, Clerk.

[Title of Court of Appeals and Cause.]

STIPULATION REGARDING EXHIBIT A

It Is Hereby Stipulated, by and between the parties hereto, through their respective attorneys of record, that Exhibit A, the Administrative Record of the Immigration and Naturalization Service, need not be printed and may be considered in its original form.

Dated: August 4, 1958.

LAUGHLIN E. WATERS,
United States Attorney,
RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,
NORMAN R. ATKINS,
Assistant U. S. Attorney,
/s/ NORMAN R. ATKINS,
Attorneys for Appellant.

HARLIN M. FULLER,
/s/ HARLIN M. FULLER,
Attorney for Appellee.

[Endorsed]: Filed August 22, 1958. Paul P. O'Brien, Clerk.

No. 15,007

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

[illegible] District Director of Immigration and Naturalization Service, Los Angeles, California,

Appellant,

vs.

[illegible] Pitman,

Appellee.

APPELLANT'S OPENING BRIEF.

[illegible] R. Watson,
United States Attorney,

[illegible] L. Lavine,
Assistant U. S. Attorney,
Chief of Civil Division,

[illegible] L. Jamison,
Assistant U. S. Attorney,
[illegible] Building,
Los Angeles 12, California,
Attorneys for Appellant.

FILED

Nov 24 1958

PAUL P. O'BRIEN, CL

[illegible] Law Printing, Los Angeles, Phone [illegible]

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No. 16107

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

RICHARD C. HOY, District Director of Immigration and Naturalization Service, Los Angeles, California,

Appellant,

vs.

MANUEL MENDOZA-RIVERA,

Appellee.

APPELLANT'S OPENING BRIEF.

Jurisdiction.

Appellee, plaintiff below, brought an action in the District Court seeking judicial review of an order of deportation [R. 3-8].[1] Jurisdiction there was invoked pursuant to 28 U. S. C. 2201 (the Declaratory Judgment Act) and 5 U. S. C. 1009 (Section 10 of the Administrative Procedures Act).

Since the judgment of the District Court [R. 26-27] was a final decision, this Honorable Court has jurisdiction of an appeal from that decision pursuant to 28 U. S. C. Secs. 1291 and 1294(1).

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[1]"R." refers to the printed Transcript of Record.

Statement of the Case.

On July 3, 1957, appellee filed a "Petition for Judicial Review of Order of Deportation and Declaratory Judgment" [R. 3-7]. In his petition appellee, a Mexican alien, alleged that in 1952 he was convicted under Section 11500 of the Health and Safety Code of California for possession of marihuana; that he had last entered the United States from Mexico in 1955 and that subsequently, on April 12, 1957, he was ordered deported from the United States because of his 1952 conviction; that on May 20, 1957, the Board of Immigration Appeals affirmed the order of deportation and directed that appellee's appeal be dismissed; that appellee therefore had exhausted his administrative remedies [R. 7]; and, finally, that the order of deportation erroneously applied Section 241(a)(11) of the Immigration and Nationality Act [8 U. S. C. 1251-(a)(11)] in that the statute provided for the deportation of an alien convicted of possessing "narcotic drugs," when, in fact, plaintiff had been convicted of possessing "marihuana." Appellee's petition concluded with the prayer that the deportation "record" be reviewed, that the Court enter judgment that he was not deportable, and that appellant Hoy be restrained from effectuating appellee's deportation from the United States [R. 7].

Appellant, on August 9, 1957, answered with a general denial [R. 8-10].

The pretrial order [R. 11-14], filed on November 4, 1957, recited the foregoing [R. 12-13] as admitted facts, leaving only issues of law to be litigated [R. 13-14]. These issues were: First, whether Congress in the Narcotic Control Act of 1956 intended by amending Section 241(a)(11) of the Immigration and Nationality Act to

distinguish between "narcotic drugs" and "marihuana," and, secondly, whether state statutes controlled in applying the amended Section 241(a)(11)'s use of the phrase ". . . possession of . . . narcotic drugs."

The Honorable Harry C. Westover, in a written opinion filed February 24, 1958 [R. 15-20], held ". . . that Congress did not intend to include marihuana within the definition of narcotic drugs" [R. 19].[2] Thereafter, the judgment was entered on March 10, 1958 [R. 27], granting appellee his requested relief.

On April 24, 1958, appellant filed his notice of appeal.

Statement of Points.

The District Court erred as a matter of law when it construed "narcotic drugs" as used in 8 U. S. C. 1251-(a)(11), as amended, in the phrase ". . . who at any time has been convicted of a violation of . . . any law or regulation relating to the illicit possession of . . . narcotic drugs" as not including "marihuana."

Question Presented.

Is "marihuana" included within the "narcotic drugs" provision of Title 8 U. S. C. Sec. 1251(a)(1) which reads ". . . who at any time has been convicted of a violation of . . . any law or regulation relating to the illicit possession of . . . narcotic drugs . . ."?

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[2]Subsequently, the Honorable William C. Mathes, in a different case presenting the same legal issues, reached the same conclusion, relying solely on this precedent set by Judge Westover. The Government's opening appeal brief in that case, *Hoy v. Rojas-Gutierrez,* C. A. No. 16105, was filed in this Honorable Court on October 24, 1958.

Statutes Involved.

Title 8 U. S. C. 1251(a), insofar as pertinent, reads:

> "Any alien in the United States . . . shall, upon the order of the Attorney General, be deported who —" 66 Stat. 204; enacted June 27, 1952.

Title 8 U. S. C. 1251(a)(11) was amended by Section 301(b), Public Law 728, 70 Stat. 575, July 18, 1956, to read as follows:

> "(11) is, or hereafter at any time after entry has been, a narcotic drug addict, or who at any time has been convicted of a violation of, *or a conspiracy to violate,* any law or regulation relating to the illicit *possession of or* traffic in narcotic drugs, or who has been convicted of a violation of, *or a conspiracy to violate,* any law or regulation governing or controlling the taxing, manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation, exportation, or the possession for the purpose of manufacture, production, compounding, transportation, sale, exchange, dispensing, giving away, importation, or exportation of opium, coca leaves, heroin, marihuana, any salt derivative or preparation of opium or coca leaves or isonipecaine or any addiction-forming or addition-sustaining opite;" [The italicized words are the words added by amendment in Public Law 728; otherwise the section reads as when it was enacted as part of 8 U. S. C. 1251(a) on June 27, 1952.]

ARGUMENT.

I.

Public Law 728 Clearly Shows That Congress Regarded "Marihuana" and "Narcotic Drugs" Violators to Be in Pari Delicto and Intended That the Statutes' Sanctions Be Applied Indiscriminately to Both Classes of Offenders.

Initially, it must be conceded, that nowhere in Public Law 728 does Congress expressly define "narcotic drugs" or "marihuana" and, indeed, even therein refers conjunctively to "narcotic drugs and marihuana." Thus, to cite a single example, Public Law 728 itself is described as an Act ". . . to provide for a more effective control of narcotic drugs and marihuana and for other related purposes." (70 Stat. 567.) Further, in substantive criminal statutes, Congress has definitionally differentiated between "narcotic drugs" (26 U. S. C. 4731) and "marihuana" (26 U. S. C. 4761). Yet, this is not a universal distinction. Thus, for civil purposes, in 42 U. S. C. 201(j) and 49 U. S. C. 787(d), Congress included "marihuana" (or "Indian hemp") in its definitions of "narcotics" or "narcotic drugs." However, in Title 8 U. S. C. (viz. Secs. 1182(a)(23) and 1251(a)(11)) Congress uses "narcotic drugs" and "marihuana" without expressly defining the terms.[3]

What was the purpose of Public Law 728, or "The Narcotic Control Act of 1956"?[4] Quite clearly it was prompted

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[3]It will be argued *infra* that the omission of the "narcotic drug" definition is both significant and deliberate. Congress, then, depending upon the intended purpose of particular legislation, may define "narcotic drugs" independently of "marihuana," as including "marihuana," or not at all.

[4]70 Stat. 567.

by a social problem Congress thought to be critical—the "narcotics problem."[5] If for Federal criminal statutes Congress has recognized a theoretical dissimilarity between "marihuana" and "narcotic drugs," Congress has surely shown that in terms of their practical social consequences it regards "marihuana" and "narcotic drugs" as Siamese twins. For it is together and not singly that these substances and their traffic constitute the "narcotics problem." Compare *Caudillo v. United States,* 253 F. 2d 513 (9 Cir., 1958). It is apparent from Public Law 728, 70 Stat. 567 *et seq.,* that Congress intended to deal equally with the marihuana and the narcotic drug offender.

That Congress regarded the marihuana and narcotic drug trafficker to be equally dangerous, and further intended that the same consequences befall them both, is nowhere better illustrated than in the penalty provisions of Federal Criminal Statutes relating to marihuana (*e.g.,* 21 U. S. C. 176(a)) or narcotic drugs (*e.g.,* 21 U. S. C. 174). With certain exceptions, sentences imposed for either violation are mandatory, 26 U. S. C. 7237; Sec. 103 Pub. Law 728, 70 Stat. 568. These penalty provisions, regardless of the substance dealt in, are equally severe.

It is certainly reasonable to conclude therefore, in face of this graphic display of legislative intent, that Congress desired to deport aliens convicted of "narcotics" violations, without any regard whatsoever to the identity of the substances involved, as another effective way of dealing with the "narcotics problem." To say that in 8 U. S. C.

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[5]". . . [The] illicit traffic in narcotic drugs and marihuana and their illegal uses" constitutes ". . . one of the most serious social problems confronting the American public today." H. R. 2388; 2 U. S. Cong. & Admin. News, 1956, at p. 3280.

1251(a)(11) Congress did not intend "marihuana" to be included within the meaning of ". . . illicit possession of . . . narcotic drugs" is to flout the congressional intent of the Narcotics Control Act of 1956. Such a construction by the barest of technicalities bestows an unintended and undesirable bonanza. Such a construction compels the absurd conclusion that Congress intended to smile upon the alien convicted of illegally possessing marihuana, and simultaneously to frown on the alien convicted of illegally possessing say, heroin. Clearly such an anomaly should be avoided. Congress, in Public Law 728, obviously desired to achieve broad social ends and the amending sections of Public Law 728 should therefore be broadly construed. Since Title 8 does not expressly define "narcotic drugs" it is submitted that Congress, to achieve its purpose, intended that "narcotic" be given its lay meaning: "A drug which in moderate doses allays sensibility, relieves pain, and produces profound sleep, but which in poisonous doses produces stupor, coma, or convulsions. Among the chief narcotics are 'opium (with morphine), belladonna (with atropine), Indian hemp (*i.e.,* marihuana), strumonium and hyoscyasmis,' " *Webster's New International Dictionary,* 2d Ed. 1956.

II.

Congress Intended That the 8 U. S. C. 1251(a)(11) Phrase, "Possession of Narcotic Drugs," Incorporate State Criminal Statutes' Definition of "Narcotic Drugs."

Prior to his deportation hearing, appellee had been convicted of violating Section 11500 of the Health and Safety Code of California which provides, among other things, that ". . . no person shall possess . . . a narcotic [with inapplicable exceptions]." Section 11001 of that same

Code states that "narcotics . . . means any of the following . . . (h) all parts of the plant *Cannabis Sativa L.* (commonly known as marihuana). . . ." While California is apparently not among the forty-four states and three territories that have enacted the Uniform Drug Act (see 9B Uniform Laws Annotated 729), it nevertheless has enacted the definition section of the Uniform Drug Act, 9B U. L. A. Sec. 1, at page 281. However, the point of this apparent digression is that if "narcotic drugs" in the Section 1251(a)(11) phrase "illicit possession of . . . narcotic drugs" depends on state statutes for its interpretations, the order of deportation is valid and the judgment below should be reversed.

The pertinent portion of Title 8, U. S. C. 1251(a)(11) relates to the deportation of an alien convicted of ". . . any law . . . relating to the illicit possession of . . . narcotic drugs." By the use of the word "any" Congress obviously meant state "law[s]" relating to the illicit possession of "narcotic drugs." Congress could not have meant federal criminal laws or statutes because there is no federal crime *per se* for the mere possession of either narcotic drugs or marihuana. If Congress, in Title 8, had expressly provided a definition of "narcotic drugs" that definition naturally would have controlled in applying state laws (*Nicholson v. United States,* 141 F. 2d 552 (9 Cir., 1944)). But, in absence of such an express federal definition, "narcotic drugs" must, if the words "possession of" are to be given meaning, refer to the applicable state laws. The reason Congress did not expressly define "narcotic drugs" in 8 U. S. C. 1251(a)(11), it is submitted, is that full effect could thereby be given to the various state statutory definitions thereof. (*United States v. Eramdjian,* 155 Fed. Supp. 914, 931 (S. D. Cal. 1957).)

Conclusion.

In conclusion, appellant respectfully submits to this Honorable Court:

1. That the whole import and purpose of Public Law 728, 70 Stat. 567, was to deal harshly and indiscriminately with both narcotic drugs and marihuana offenders, including the deportation of aliens so convicted either in state or federal courts; and
2. That in any event, the Narcotic Control Act's amendment of 8 U. S. C. 1251(a)(11) to read "illicit possession of . . . narcotic drugs" was designed to incorporate state statutory definitions of "narcotic drugs," including such definitions that incorporated "marihuana"; and

Hence, for either or both of these reasons the judgment appealed from below should be reversed.

Respectfully submitted,

LAUGHLIN E. WATERS,
United States Attorney,

RICHARD A. LAVINE,
Assistant U. S. Attorney,
Chief of Civil Division,

HENRY P. JOHNSON,
Assistant U. S. Attorney,
Attorneys for Appellant.

No. 16107.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

RICHARD C. HOY, District Director of Immigration and Naturalization Service, Los Angeles, California,

Appellant,

vs.

MANUEL MENDOZA-RIVERA,

Appellee.

APPELLEE'S BRIEF.

HARLIN M. FULLER,
610 South Broadway,
Los Angeles 14, California,
Attorney for Appellee.

FILE
DEC 17 195
PAUL P. O'BRIEN

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No. 16107.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

RICHARD C. HOY, District Director of Immigration and Naturalization Service, Los Angeles, California,

Appellant,

vs.

MANUEL MENDOZA-RIVERA,

Appellee.

APPELLEE'S BRIEF.

Jurisdiction.

The jurisdictional facts are set forth in Appellant's Opening Brief (p. 1) and are adopted by Appellee.

Statement of the Case.

The statement of the case is adequately set forth in Appellant's Opening Brief (pp. 2-3).

Question Presented.

The question presented as stated in Appellant's Opening Brief (p. 3) is correct, except that Appellant inadvertently stated that the applicable section of the law pertaining to the question presented is Title 8 U. S. C. Sec. 1251(a)(1), whereas the applicable section is Title 8 U. S. C. Sec. 1251(a)(11).

ARGUMENT.

I.

Public Law 728 and House Report No. 2388, June 19, 1956, Accompanying H. R. 11619, Shows That Congress Treated "Marihuana" as a Substance Not to Be Included Within the Term "Narcotic Drugs."

Throughout Public Law 728, 84th Congress, 2nd Session, Congress was careful to make a distinction between the terms "narcotic drugs" and "marihuana" and where reference is made to both the expression "narcotic drugs and marihuana" is used. For example, Sections 101 and 102 of Title 1 pertain to marihuana only, whereas Section 103 of Title 1 pertains to narcotic drugs and marihuana, and both terms are used.

Appellant, in his Opening Brief (at p. 5) states that it must be conceded that nowhere in Public Law 728 does Congress expressly define "narcotic drugs" or "marihuana." However, Section 201 of Title 2 of Public Law 728 amends Part I of Title 18 of the United States Code by inserting after Chapter 67 a new Section 1407. This new section refers to ". . . narcotic drugs as defined in Section 4731 of the Internal Revenue Code of 1954, as amended . . ." Congress has defined "narcotic drugs," omitting "marihuana" from its definition (26 U. S. C. 4731) and has defined "marihuana" without including in that definition any substance included in its definition of "narcotic drugs" (28 U. S. C. 4761). The Internal Revenue Code of 1954, subchapter A of Chapter 39, is entitled "Narcotic Drugs And Marihuana." Part I of this subchapter pertains to narcotic drugs, Part II pertains to marihuana, and Part III contains miscellaneous provisions relating to narcotic

drugs and marihuana. The Food and Drugs Act, Title 21 U. S. C. 171(a), for its purposes in treating of the subject narcotic drugs, defines the term "narcotic drugs" but does not include marihuana in the definition.

House Report No. 2388, 84th Congress, 2nd Session, June 19, 1956, accompanying H. R. 11619, reported in No. 13, 1956 *U. S. Code Congressional And Administrative News,* at pages 4288-4329, distinguishes between the terms "narcotic drugs" and "marihuana," by referring to "marihuana" alone, for example, at pages 4288 and 4289, and to "narcotic drugs and marihuana," page 4289, and to "Federal narcotic or marihuana laws," page 4289. The Conference Report, No. 2546, 84th Congress, 2nd Session, June 29, 1956, of the two Houses, accompanying H. R. 11619, reported in *U. S. Code Congressional And Administrative News, supra,* at pages 4329 to 4336, distinguishes between the two terms, as does the House Report.

Appellant, in his Opening Brief, cites 42 U. S. C. 201(j) and 49 U. S. C. 787(d) as evidence that Congress included "marihuana" in its definition of "narcotics" or "narcotic drugs" for civil purposes. However, as to the first citation, marihuana was included in the definition as a matter of convenience and to avoid repetition in the treatment of the subject of the Public Health Service, and the same is true as to the second citation, in the treatment of the subject of contraband articles and, as to the second citation, it was acknowledged that "narcotic drug" and "marihuana" have each been defined separately by the Congress as hereinabove stated.

It is evident that Congress, in its treatment of the terms "narcotic drugs" and "marihuana" distinguished between the two, passed legislation on one without the

other, and in considering both terms at the same time referred to both. It is contended that if Congress had contemplated including marihuana with narcotic drugs in the provisions of Title 8 U. S. C. Section 1251(a)(11) pertaining "to the illicit possession" it would have done so clearly and concisely as Congress has done in other instances in enacting legislation where the two terms are considered together.

II.

Congress Could Not Have Intended That 8 U. S. C. 1251(a)(11) "Possession of Narcotic Drugs" Incorporate State Criminal Statutes' Definition of "Narcotic Drugs."

Appellant points out that Appellee was convicted of possession of marihuana in violation of Section 11500 of the Health and Safety Code of California, and that Section 11001 of that same Code includes marihuana within the meaning of the term "narcotics." Appellant then takes the position that the reason Congress did not expressly define "narcotic drugs" in 8 U. S. C. 1251(a)(11), ". . . is that full effect could thereby be given to the various state statutory definitions thereof," and cites *United States v. Eramdjian,* 155 Fed. Supp. 914, 931 (S. D. Cal. 1957) (page 8, Appellants Opening Brief). However, if Congress intended to rely on a state's definition of narcotic drugs, the whole purpose of 8 U. S. C. 1251(a)(11) could be defeated. It is conceivable that a state could include numerous substances unrelated to any concept of the term "narcotic drugs" or the term "narcotic" for the purpose of establishing a criminal section pertaining to the possession of substances which the state felt should be declared unlawful. An alien convicted of the illicit possession of such a sub-

stance could then be deported from the United States if Appellant's contention is correct. Certainly Congress could not have intended that the Federal statute in question should be dependent on state statutory definitions of the term "narcotic drugs."

The United States Supreme Court, in its opinion in *Jerome v. United States,* 318 U. S. 101, 104, states:

> "At times it has been inferred from the nature of the problem with which Congress was dealing that the application of a federal statute should be dependent on state law. . . . But we must generally assume, in the absence of a plain indication to the contrary, that Congress when it enacts a statute is not making the application of the federal act dependent on state law. That assumption is based on the fact that the application of federal legislation is nationwide (*United States v. Pelzer,* 312 U. S. 399, 402) and at times on the fact that the federal program would be impaired if state law were to control."

See also, *Textile Workers v. Lincoln Mills,* 353 U. S. 448, 457; and *Board of Commissioners v. United States,* 308 U. S. 343, 351-352.

Conclusion.

In conclusion, Appellee respectfully submits to this Honorable Court:

1. That Congress has distinguished between the terms narcotic drugs and marihuana and therefore could not have intended to include a violation of law relating to the illicit possession of marihuana as a violation of law relating to the illicit possession of narcotic drugs under 8 U. S. C. 1251(a)(11) as amended by Public Law 728; and

2. That Congress did not intend that the term narcotic drugs should depend upon state statutory definitions; and

3. That the conviction of the mere possession of marihuana is not a basis for an order of deportation under this statute.

The judgment of the trial court should therefore be affirmed.

Respectfully submitted,

HARLIN M. FULLER,

Attorney for Appellee.

No. 16108

United States Court of Appeals

for the Ninth Circuit

CORNELI SEED COMPANY, a corporation,
Appellant,

vs.

UNION PACIFIC RAILROAD COMPANY, a corporation,
Appellee.

Transcript of Record

Appeal from the United States District Court for the District of Idaho, Southern Division

FILED
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No. 16108

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United States District Court, For The District of Idaho, Southern Division

Civil No. 3148

UNION PACIFIC RAILROAD COMPANY, a corporation, Plaintiff,

vs.

CORNELI SEED COMPANY, INC., a corporation, Defendant.

COMPLAINT

Comes now Union Pacific Railroad Company, a corporation, and for cause of action against the defendant alleges:

I.

That this action arises under the Interstate Commerce Act, Title 49 USCA 6, and jurisdiction is conferred under Title 28 USCA, Section 1337. That the Union Pacific Railroad Company is a corporation duly organized and existing under and by virtue of the laws of the State of Utah and authorized to transact business in the State of Idaho. That the defendant is a corporation duly organized and existing under and by virtue of the laws of the State of Idaho and that the amount in controversy exceeds the sum of $3,000.00, exclusive of interest and costs.

II.

That the Corneli Seed Company, Inc., during February and March, 1953, delivered to the plaintiff at Twin Falls, Idaho, nine carloads of beans, peas or shelled corn for transportation to various

points outside the State of Idaho; that said shipments, showing initial and car numbers, date of shipment, consignee and destination, are as follows:—

GBW 778, Feb. 25, 1953—Corneli Seed Company, Inc., St. Louis, Mo.

CG 6568, Mar. 24, 1953—Illinois Canning Co., Fowler, Ind.

NYC 177634, Mar. 19, 1953—Rockfield Farms, Inc., Rockfield, Wisc.

Erie 86142, Mar. 17, 1953—Stokely-VanCamp, Inc., Columbus, Wisc.

CG 41065, Mar. 10, 1953—St. Mary's Packing Co., North Freedom, Wisc.

NYC 31350, Mar. 17, 1953—Stokely-VanCamp Inc., Columbus, Wisc.

T&P 40606, Mar. 14, 1953—Fox Valley Canning Company, Harborville, Wisc.

B&O 278828, Mar. 12, 1953—Riverside Truck & Storage Co., Bay City, Mich.

SP 101509, Mar. 9, 1953—Oostburg Canning Co., Oostburg, Wisc.

That said shipments were by the plaintiff and its connecting carriers transported from Twin Falls, Idaho, to the various destinations shown.

III.

That on April 15, 1953, the defendant filed with the plaintiff its claim for refund on each shipment of a portion of the transportation charges paid, asserting that as to each shipment transit privi-

leges should have been allowed, and which, if allowed, would materially reduce the rate charged and paid by the defendant. That on the basis of said claims the plaintiff made refunds to the defendant in June and July, 1953, in varying amounts on all shipments, and in the order said shipments are listed above said refunds were as follows:—

Freight Charges	Federal Tax	Total
$ 239.27	$ 7.18	$ 246.45
380.47	11.41	391.88
283.27	8.50	291.77
385.03	11.55	396.58
471.39	14.14	485.53
387.02	11.62	398.64
382.42	11.48	393.90
386.88	11.61	398.49
303.42	9.10	312.52
$3,219.17	$96.59	$3,315.76

IV.

That shortly after said refunds had been made plaintiff discovered that the defendant had not complied with the applicable tariff provisions relating to transit privileges, and that instead of recognizing defendant's claims said claims should have been declined. That said refunds are contrary to tariff provisions and were therefore erroneously made.

V.

That there is also due and owing the plaintiff from the defendant additional freight charges re-

sulting from erroneous application of the lawful tariff rate, as follows:—

On shipment loaded in Car CG 6568, additional freight charges of $7.38, and Federal Tax of 22c.

On shipment loaded in Car NYC 177634, additional freight charges of $132.77, and Federal Tax of $3.98.

On shipment loaded in Car B&O 278828, additional freight charges of 57c, and Federal Tax of 2c.

That on shipment loaded in Car T&P 40606 there was an overcharge made of freight charges in the amount of $16.70, and Federal Tax of 50c, which amounts when deducted from the foregoing undercharges, leaves a net balance due of $124.02, and Federal Tax of $3.72, in addition to the amount set forth in paragraph III above.

That there is now due and owing from the defendant the sum of $3,443.50, no part of which has been paid, although demand has been made upon the defendant to do so.

Wherefore, plaintiff prays judgment against the defendant in the sum of $3,443.50, with interest at the rate of 6% from the 2nd day of July, 1953, together with plaintiff's costs herein incurred.

/s/ BRYAN P. LEVERICH,
/s/ L. H. ANDERSON,
/s/ E. C. PHOENIX,
Attorneys for Plaintiff.

[Endorsed]: Filed January 19, 1955.

[Title of District Court and Cause.]

SUMMONS

To the above named Defendant:

You are hereby summoned and required to serve upon Bryan P. Leverich, 10 South Main St., Salt Lake City, Utah; and L. H. Anderson and E. C. Phoenix, P. O. Box 530, Pocatello, Idaho, plaintiff's attorneys, an answer to the complaint which is herewith served upon you, within 20 days after service of this summons upon you, exclusive of the day of service. If you fail to do so, judgment by default will be taken against you for the relief demanded in the complaint.

Date: January 19, 1955.

[Seal] ED. M. BRYAN,
Clerk of Court.

/s/ LONA MANSER,
Deputy Clerk.

Return On Service of Writ

I hereby certify and return, that on the 20th day of January, 1955, I received this summons and served it together with the complaint herein as follows: By showing the Original to and handing to and leaving a true and correct copy of Summons & Complaint thereof with Ralph R. Breshears, Mgr. Agent for Corneli Seed Company, Inc., a Corporation. This was done in room 309

Idaho Bldg. at 11:30 A.M. on January 20, 1955.
Marshal's Fees

SAUL H. CLARK,
United States Marshal.
/s/ By REX WALTERS,
Deputy United States Marshal.

Travel: None.
Service: $2.00.

$2.00

[Endorsed]: Filed January 24, 1955.

[Title of District Court and Cause.]

STIPULATION

It Is Hereby Stipulated by and between the parties hereto, through their respective counsel, that the defendant in the above entitled case may have twenty days from and after a decision is rendered by the Interstate Commerce Commission upon a complaint filed with said Commission by the defendant requesting authority to waive some or all of the freight charges referred to in plaintiff's complaint.

Dated This 28th day of January, 1955.

/s/ BRYAN P. LEVERICH,
/s/ L. H. ANDERSON,
/s/ E. C. PHOENIX,
Attorneys for Plaintiff.
/s/ RALPH R. BRESHEARS,
Attorneys for Defendant.

ORDER

Upon reading the above stipulation, good cause appearing therefor, It Is Ordered that the defendant herein may have twenty days from and after the decision of the Interstate Commerce Commission in which to plead to the complaint herein.

Dated This January 28, 1955.

/s/ FRED M. TAYLOR,
District Judge.

[Endorsed]: Filed January 28, 1955.

[Title of District Court and Cause.]

ANSWER OF DEFENDANT CORNELI SEED COMPANY, INC.

Now comes the defendant Corneli Seed Company, Inc. and for its answer to plaintiff's complaint states as follows:

I.

Defendant admits so much of paragraph I of plaintiff's complaint as alleges that plaintiff is a corporation duly organized and existing under the laws of the State of Utah and authorized to transact business in the State of Idaho, that defendant is a corporation organized and existing under the laws of the State of Idaho, and that the amount in controversy exceeds the sum of $3,000.00 exclusive of interest and costs; and defendant denies all other allegations of said paragraph I.

For further answer to paragraph I, defendant

states that jurisdiction is conferred under Title 28 USCA, Section 1332, in that plaintiff and defendant are citizens of different states and the matter in controversy exceeds the sum or value of $3,000.00, exclusive of interest and costs.

II.

Defendant admits the averments of paragraph II of plaintiff's complaint, and for further answer thereto states that said shipments were transit shipments and so recorded by plaintiff on their arrival at Twin Falls, Idaho, from their respective points of origin; that said shipments were forwarded by plaintiff to their final destinations, as specified in plaintiff's complaint, all in accordance with a course of claim procedure and settlement previously established between plaintiff and defendant and then and there in force and effect, all as hereinafter more particularly set out.

III.

Defendant admits the averments of paragraph III of plaintiff's complaint, and for further answer thereto states that said claim was filed by defendant and paid by plaintiff in recognition of and in accordance with the course of claim procedure and settlement previously established between plaintiff and defendant and then and there in force and effect, all as hereinafter more particularly set out.

IV.

Defendant denies the averments of paragraph IV of plaintiff's complaint.

V.

Defendant admits so much of paragraph V of plaintiff's complaint as alleges that it owes plaintiff additional freight charges and taxes in the net aggregate amount of $127.74 resulting from erroneous application of the applicable tariff rates on the four shipments specified in said paragraph V but defendant denies each and every other averment contained in said paragraph V.

VI.

For its further answer, defendant states as follows:

(A) That at all times mentioned in plaintiff's complaint and for a long time prior thereto, defendant has been engaged in the business of processing and wholesaling seed; that in the course of said business defendant purchased seed from producers located within and without the State of Idaho and caused such seed to be transported by plaintiff and its connecting carriers to Twin Falls, Idaho, where said seed was stopped in transit for cleaning and processing by defendant, and then forwarded by plaintiff and its connecting carriers to defendant's customers; that such shipments are known as transit shipments and as such are entitled to the plaintiff's single factor transit rates; that plaintiff's rules and regulations specify that the outgoing bills of lading of such transit shipments should, among other things, indicate the place of origin of the seeds shipped; that from 1944 to 1949 the outgoing bills of lading of such shipments so indicated the

origin of such seed; that by reason of such notations on the outgoing bills of lading, defendant's customers ascertained and determined defendant's sources of supply and thereupon purchased their requirements directly, thereby depriving defendant of valuable business; that commencing in 1949, representatives of plaintiff and of defendant agreed or at least pursued a course of claim procedure and settlement with respect to such transit shipments which would not require notation on outgoing bills of lading of the points of origin of the seeds shipped; that said course of claim procedure and settlement called for defendant to pay the transportation charges for shipments into and out of Twin Falls, Idaho, at the full rates and then to file claims for refund of the excess so paid over the transit rates, furnishing with such claims information as to points of origin of the shipments; that plaintiff and defendant followed such course of claim procedure and settlement from 1949 to December 15, 1953 at which time plaintiff notified defendant that subsequent investigation of the claims on which plaintiff had made refunds in June and July, 1953 (as alleged in paragraph V of the complaint herein) had developed that the basis of claim settlement was not applicable because of non-compliance with transit rules and requested that the refunds which had been made be returned.

(B) That the shipments mentioned in paragraph II of plaintiff's complaint and on which refunds were made as alleged in paragraph III of the

complaint were recorded for transit by plaintiff on arrival at Twin Falls, Idaho, prior to their forwarding as described in plaintiff's complaint; that said shipments were entitled to plaintiff's single factor transit rates; that defendant made claims for the transit rate and plaintiff honored the same, all in accordance with the course of claim procedure and settlement alleged in section (A) above.

(C) That the shipments mentioned in plaintiff's complaint were in truth and fact transit shipments and were so known to be by plaintiff at the time it paid defendant's claims for refund of the amounts paid by defendant in excess of the transit rate.

Wherefore, having made full answer to plaintiff's complaint, defendant prays that the prayer of plaintiff's complaint except to the extent of $127.74 as to which amount defendant admits liability be denied and plaintiff's action except as to said $127.74 be dismissed, and that defendant be discharged without costs.

/s/ RALPH R. BRESHEARS,
GREENSFELDER, HEMKER & WIESE,

/s/ By EDWARD L. WIESE,
Attorneys for Defendant.

Acknowledgment of Service Attached.

[Endorsed]: Filed September 11, 1957.

[Title of District Court and Cause.]

AGREED STATEMENT OF FACTS

It Is Hereby Stipulated and Agreed by and between the parties hereto through their respective counsel:

I.

That this action arises under the Interstate Commerce Act, Title 49 USCA 6, and jurisdiction is conferred under Title 28 USCA, Section 1337, and also under Title 28 USCA, Section 1332, in that the Union Pacific Railroad Company is a corporation duly organized and existing under and by virtue of the laws of the State of Utah and authorized to transact business in the State of Idaho. That the defendant is a corporation duly organized and existing under and by virtue of the laws of the State of Idaho and that the amount in controversy exceeds the sum of $3,000.00, exclusive of interest and costs.

II.

That defendant since at least January 5, 1944 and up to and including December 15, 1953, has been engaged in the business of processing and wholesaling seeds, including shelled corn, dried beans and peas; that in the course of said business defendant purchased seeds from various growers, producers and processors at points in California, Idaho, Oregon and Washington; that defendant caused such seeds to be shipped in carload lots from their respective points of origin, by plaintiff and its connecting carriers, to Twin Falls, Idaho, where

they were stopped in transit and subsequently forwarded, at defendant's instructions, by plaintiff and its connecting carriers to destinations in Florida, Indiana, Michigan, Missouri, New York, Tennessee, and Wisconsin; that said seeds were stopped in transit at Twin Falls, Idaho, to permit defendant to clean and otherwise process the same at its plant in Twin Falls, Idaho.

III.

That the rules and regulations of the transit tariff of the plaintiff applicable to the shipments involved herein provided that when shipments are forwarded from the transit station, in this case Twin Falls, Idaho, unexpired inbound freight bills which had been recorded, or tonnage credit slips must be surrendered and cancelled; that the outbound bills of lading or shipping orders must have inserted thereon the weight, point of origin, and date of each inbound shipment covering the commodities forwarded and that the transit rate would not apply if shippers fail or decline to comply with all such rules and regulations; that the combination of rates from points of origin of defendant's seeds to Twin Falls, Idaho, and from Twin Falls, Idaho, to points of final destination, exceeded the respective single-factor through rates from points of origin to points of destination plus the applicable transit charge; that the through or single-factor transit rate was a less expensive method for defendant to ship its seeds.

IV.

That for several years beginning at least as early as January 5, 1944, the defendant complied with the tariff provision above stated and obtained the benefit of the transit or single-factor rates; that compliance with said tariff in part required notation on the outbound bills of lading forwarded to defendant's customers of the points of origin of the seeds sold by defendant to those customers and thus enabled those customers to ascertain and locate defendant's producers and sources of supply and to purchase from them direct, with a consequent loss of business to defendant; that in order to effect discontinuance of this practice by defendant's customers, sometime in January or February, 1949, the local representative of defendant adopted and thereafter pursued a practice of making shipments out of the transit point (Twin Falls, Idaho) by using the regular forms of bill of lading which are used for shipments not entitled to transit privileges and which did not show the information previously shown in compliance with the transit tariff and then filed with the plaintiff overcharge claims attached to which were copies of the bill of lading for the outbound shipment, a memorandum bill marked "for transit consideration only" which contained inbound references, and a statement showing a computation of the difference between the transit rate and the combination rate, that is to say, such claims were for the difference between the transit or through single-factor rate from original point of shipment to final destination, and the

combination of the rate from original point of shipment into Twin Falls, Idaho, and the rate from Twin Falls, Idaho, to destination, the combination rate being the greater; that thereafter plaintiff paid claims so submitted which had the result of making the effective rate of defendant's true transit shipments exactly what plaintiff's transit tariff authorized. Defendant's local representative at Twin Falls, Idaho, who adopted and pursued the practice of making shipments and filing claims as above set forth was not informed as to all of the rules and regulations of the applicable transit tariff nor did he have the ability to interpret said tariff, and at no time was he informed by plaintiff's representatives at Twin Falls, Idaho, that the practice and procedure which he had adopted was not proper or adequate, and at no time did said representatives of plaintiff object to said practice or the claims filed, nor did they inform said local representative of defendant that provisions of the transit tariff were not being complied with; and that said conditions continued to obtain until the nine shipments detailed in paragraph V hereof.

V.

That the Corneli Seed Company, Inc., during February and March, 1953, delivered to the plaintiff at Twin Falls, Idaho, nine carloads of beans, peas or shelled corn for transportation to various points outside the State of Idaho; that said shipments, showing initial and car numbers, date of shipment, consignee and destination, are as follows:

GBW 778, Feb. 25, 1953—Corneli Seed Company, Inc., St. Louis, Mo.

CG 6568, Mar. 24, 1953—Illinois Canning Co., Fowler, Ind.

NYC 177634, Mar. 19, 1953—Rockfield Farms, Inc., Rockfield, Wisc.

Erie 86142, Mar. 17, 1953—Stokely-VanCamp, Inc., Columbus, Wisc.

CG 41065, Mar. 10, 1953—St. Mary's Packing Co., North Freedom, Wisc.

NYC 31350, Mar. 17, 1953—Stokely-VanCamp, Inc., Columbus, Wisc.

T&P 40606, Mar. 14, 1953—Fox Valley Canning Company, Harborville, Wisc.

B&O 278828, Mar. 12, 1953—Riverside Truck & Storage Co., Bay City, Mich.

SP 101509, Mar. 9, 1953—Oostburg Canning Co. Oostburg, Wisc.

That said shipments were by the plaintiff and its connecting carriers transported from Twin Falls, Idaho, to the various destinations shown.

VI.

That on April 15, 1953, the defendant filed with the plaintiff its claim for refund on each shipment of a portion of the transportation charges paid, asserting that as to each shipment the transit, or single factor rate should have been applied, and which, if used, would reduce the combination rate charged and paid by the defendant. That on the basis of said claims the plaintiff made refunds to

the defendant in June and July, 1953, in varying amounts on all shipments, and in the order said shipments are listed above said refunds were as follows:

Freight Charges	Federal Tax	Total
$ 239.27	$ 7.18	$ 246.45
380.47	11.41	391.88
283.27	8.50	291.77
385.03	11.55	396.58
471.39	14.14	485.53
387.02	11.62	398.64
382.42	11.48	393.90
386.88	11.61	398.49
303.42	9.10	312.52
$3,219.17	$96.59	$3,315.76

VII.

That on four of the shipments referred to in paragraph V hereof there was an erroneous application of the lawful tariff rate, resulting in undercharges on three of the shipments and an overcharge on another, as follows:

On shipment loaded in car CG 6568, additional freight charges of $7.38, and Federal Tax of 22c.

On shipment loaded in Car NYC 177634, additional freight charges of $132.77, and Federal Tax of $3.98.

On shipment loaded in Car B&O 278828, additional freight charges of 57c, and Federal Tax of 2c.

On shipment loaded in Car T&P 40606 there was an overcharge made of freight charges in the amount of $16.70, and Federal Tax of 50c, which amounts when deducted from the undercharges on the first three shipments referred to in this paragraph leaves a net balance due of $124.02, and Federal Tax of $3.72, and defendant admits that it is indebted to plaintiff in said total amount of $127.74.

VIII.

That as to each of said nine shipments detailed in paragraph V hereof transit rates were available and allowable under the applicable and lawful transit tariff, if the rules and regulations contained in said transit tariff had been complied with by the defendant at the time each shipment was made from Twin Falls, Idaho; application of said transit tariff rate would entitle defendant to net refunds of $3,188.02, the excess of the amount of $3,315.76 which were actually refunded over $127.74 admitted by defendant to be due plaintiff.

IX.

That defendant in making the nine shipments detailed in paragraph V hereof and in filing the claims for refund detailed in paragraph VI hereof followed exactly the same procedure of making shipments and filing claims which defendant had adopted and pursued since sometime in January or February, 1949, as detailed in paragraph IV hereof.

X.

That on or about December 15, 1953, the plaintiff concluded that the defendant had not complied with the applicable tariff provisions relating to transit privileges at Twin Falls, Idaho, and that instead of recognizing and paying defendant's claims as it had done on the shipments referred to in paragraph V hereof that it should have declined said claims and accordingly made demand on the defendant for repayment of the amounts refunded by plaintiff to the defendant on the nine shipments as detailed in paragraphs V and VI hereof. Defendant declined this demand and upon further demand by the plaintiff and advice that suit would be instituted to enforce collection the defendant advised plaintiff that proceedings were to be instituted before the Interstate Commerce Commission to determine the applicability, reasonableness and lawfulness of the charges upon which the within action was based.

XI.

That thereafter, and on October 1, 1954. the defendant, Corneli Seed Company, Inc., filed a complaint with the Interstate Commerce Commission against the plaintiff herein, Union Pacific Railroad Company, and other connecting carriers transporting the shipments herein referred to, which complaint was designated as "No. 31639, Corneli Seed Company, et al., vs. Atlantic Coast Line Railroad Company, et al."; that said complaint challenged the application of the rates and charges on

seeds in carloads from points in California, Idaho, Oregon and Washington to Twin Falls, Idaho, there stopped in transit, and subsequently forwarded to destinations in Florida, Indiana, Michigan, Missouri, New York, Tennessee and Wisconsin, alleging that said rates and charges were inapplicable, unjust and unreasonable, and requesting the said Commission to determine the applicable and lawful rates, and award reparation. Said proceedings related to the nine shipments referred to herein as well as five others not connected with the case at bar.

XII.

That on the 19th day of January, 1955, the plaintiff instituted this action against the defendant for the recovery of the amounts set forth herein and after summons and complaint were served on the defendant, and inasmuch as the charges set forth in plaintiff's said complaint were being investigated by the Interstate Commerce Commission, the parties hereto through their respective counsel stipulated that the defendant could have twenty days from and after the decision of the Interstate Commerce Commission in which to plead to plaintiff's complaint, and upon this stipulation this Court on January 28, 1955, made and entered an Order in conformity with the Stipulation.

XIII.

That the Interstate Commerce Commission upon the complaint filed with it, referred to above, the presentation of evidence by the parties, and the

consideration of the matter, made its Report and Order on March 27, 1956, wherein the Commission found that the tariff provisions relating to transit privileges involved herein must be observed before the defendant was entitled to transit privileges, that the Corneli Seed Company did not observe them and that the "assailed rates and charges are not shown to have been or to be inapplicable, unjust or unreasonable" and accordingly ordered dismissal of the cause. Said Report and Order of the Commission are attached hereto marked Exhibit "A" and made a part hereof.

XIV.

That after the Report and Order of the Interstate Commerce Commission was made and entered (Exhibit "A") the defendant herein, Corneli Seed Company, Inc., petitioned the Interstate Commerce Commission for reconsideration or further hearing in the matter, which Petition was by the said Commission denied on the 30th day of August, 1956, and that no further proceedings in that matter were taken or had by the said defendant.

XV.

That this Agreed Statement of Facts constitutes submission of the above entitled cause to the Court for decision and judgment as to whether the plaintiff Union Pacific Railroad Company is entitled to recover from the defendant Corneli Seed Company, Inc., the amount prayed for in plaintiff's complaint; that Findings of Fact by the Court are hereby waived.

Dated this 18th day of February, 1958.

/s/ BRYAN P. LEVERICH,
/s/ L. H. ANDERSON,
/s/ E. C. PHOENIX,
/s/ D. A. BYBEE,
Attorneys for Plaintiff.

GREENSFELDER, HEMKER & WIESE,
/s/ By EDW. L. WIESE,
/s/ RALPH R. BRESHEARS,
Attorneys for Defendant.

EXHIBIT "A"

Interstate Commerce Commission

No. 31639[1]

Corneli Seed Company, et al.

v.

Atlantic Coast Line Railroad Company, et al.

Decided March 27, 1956

Served: April 13, 1956.

1. Rates charged on seeds, in carloads, transported in stated circumstances, from points in California, Idaho, Oregon, and Washington, stopped in transit at Twin Falls, Idaho, and reforwarded

[1] This report embraces also 31639 (Sub. No. 1) Same v. Same.

Exhibit "A"—(Continued)

to destinations in Florida, Indiana, Michigan, Missouri, New York, Tennessee and Wisconsin, found applicable and not shown to have been or to be unjust or unreasonable.

2. Routes through Wells, Nev., and over the Union Pacific Railroad to and through Twin Falls, Idaho, for seeds, in carloads, transited at Twin Falls, from origins in California on the lines of the Southern Pacific Company to the same destinations, found to be impracticable routes, and established routes through Portland, Oregon, found not unreasonably long.
3. Complaints dismissed.

William E. Rosenbaum for complainants.

Charles W. Burkett, Jr., W. H. Fitzpatrick and William P. Higgins for defendants.

REPORT OF THE COMMISSION

Division 2, Commissioners Freas, Winchell, and Murphy.

By Division 2:

The modified procedure was followed. Exceptions were filed by the complainants and the defendants replied. Exceptions and requested findings not discussed in this report nor reflected in our findings or conclusions have been considered and found not justified.

The complainants are corporations engaged in the growing, processing and wholesaling of seeds. In the title complaint, filed October 1, 1954, it is al-

Exhibit "A"—(Continued)

leged that the rates[2] charged on seeds, in carloads, from points in California, Idaho, Oregon and Washington to Twin Falls, Idaho, there stopped in transit, and subsequently forwarded to destinations in Florida, Indiana, Michigan, Missouri, New York, Tennessee, and Wisconsin were inapplicable and that the rates and charges thereon were and are unjust and unreasonable. In a supplemental complaint, No. 31639 (Sub-No. 1), filed November 29, 1954, the same complainants allege further that the routes available for seed traffic from origins on the lines of the Southern Pacific Company to the eastern destinations via Twin Falls were and are unreasonably long and that rates and charges, assailed in No. 31639, were and are, unjust and unreasonable. We are asked to prescribe new routes, determine the applicable and lawful rates, and award reparation.

The seeds consist of shelled corn, dried beans and peas, all of which were stopped in transit for cleaning, drying, grading, inspection, mixing, milling, packing, sacking, sorting, splitting, storing or weighing. The charges were paid on the shipments from points of origin to Twin Falls, where they were recorded for transit. When the seeds were subsequently reforwarded, charges on the shipments embraced by the complaints were billed at the applicable rates from Twin Falls to final des-

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[2] Rates and additions thereto are herein stated per 100 pounds and do not include the general increases authorized in Ex Parte No. 175.

Exhibit "A"—(Continued)

tinations. The combinations of the rates to and from Twin Falls exceeded the respective single-factor through rates from the points of origin to the destinations plus the applicable transit charge. The latter basis is sought.

The transit privileges were and are maintained at Twin Falls on shipments over the route through Huntington, Oreg., embracing the line of the Union Pacific Railroad Company from this point, subject to a 4.5-cent out-of-line charge for the haul over this line between Minidoka, Idaho, and Twin Falls. The transit tariff provides for this charge for a maximum out-of-line haul of 250 miles. Routes are provided from origins on the Southern Pacific to eastern destinations via Ogden, Utah. Out-of-line service from Ogden to Granger, Wy., through Twin Falls exceeds 400 miles. The defendants assert that the Portland route was established to afford transit benefits to seed processors at all points across Idaho. An extensive list is given of seed concerns at 26 points in this State.

Rules and regulations of the applicable transit tariff provided that when shipments are forwarded from the transit station, unexpired inbound freight bills, which have been recorded, or tonnage credit slips must be surrendered and canceled; that the outbound bill of lading or shipping order must have inserted thereon the weight, point of origin, and date of each inbound shipment covering the commodities forwarded and that the transit rate will not apply if shippers fail or decline to comply

Exhibit "A"—(Continued)

with all rules and regulations. These provisions are similar to those in tariffs effective at points within Pacific coast, intermountain, and western trunkline territories.

For several years, beginning at least as early as January 5, 1944, the complainants complied with the tariff provisions above stated and obtained the benefit of the single-factor rates through Huntington plus the out-of-line charge. Notations of points of origin on the bills of lading forwarded to consignee disclosed the approximate sources of supply, which enabled the complainants' customers to locate the producers and buy directly from them. A new claim procedure was thereupon instituted by the complainants for the recovery of the excess in the combination rates. For example, the first overcharge claim under this procedure, filed on March 16, 1949, pertained to an outbound shipment billed February 28, 1949. Attached to the claim were a copy of the bill of lading for the outbound shipment, a memorandum bill marked "for transit consideration only," which contained inbound references, and a statement showing a computation of the difference between the charges. This claim procedure and settlement, not authorized by the applicable transit tariff, apparently was followed for several years. On December 15, 1953, the accounting department of the Union Pacific notified Corneli Seed Company, Inc., that such claim settlements are not authorized and presented bills covering nine claims previously paid, aggregating $3,-

Exhibit "A"—(Continued)

443.50. The claims had been paid during June, 1953. Corneli Seed Co., Inc., under date of January 6, 1954, filed five additional overcharge claims, aggregating $1,317.48. These claims were declined.

The inbound shipments embraced by the 14 claims were billed on and between November 10, 1952, and November 24, 1953. The applicable rates to Twin Falls during this period were: 38 cents on corn from Caldwell, Idaho; 45 cents on beans from Nampa, Idaho; 63 cents on peas from Dishman and Spokane, Wash.; 79 cents on peas from Athena, Oreg.; 127 cents on beans from Irvine, Calif., and 141 cents on beans from Spence and Ventura, Calif. Rates applicable from Twin Falls to representative destinations were: 99 cents on beans and peas to St. Louis, Mo.; 113 cents on peas and 105 cents on corn to Oostburg, Wis.; 148 cents on peas and beans to Bay City, Mich., Green, N. Y., and La Vergne, Tenn., and 121.5, 198 and 172 cents, respectively, to the same destinations, on corn; and 154 cents on beans and 159.5 cents on corn to Belle Glade, Fla.

Differences between the combination rates charged and the corresponding single-factor rates are given as follows: From Dishman to St. Louis, a combination of 162 cents was charged, 40 cents more than the single-factor rate of 122 cents. From Dishman to Oostburg and Bay City, single-factor rates of 129 and 148 cents are 47 and 63 cents less than the respective combinations. The combinations from Caldwell to several points are 38

Exhibit "A"—(Continued)

cents more than the single-factor rates. Other differences shown range from 38 to 63 cents; shipments of beans from California points, reforwarded to Belle Glade, and La Vergne after stops at Twin Falls are not included. Because of routing restrictions, only one shipment would have been entitled to the through rate. That shipment originated at Ventura and was routed via Portland, Oreg., to Twin Falls. The rate on the inbound movement was 141 cents and the rate on the outbound movement to La Vergne was 148 cents. The latter factor is the same as the through rate from Ventura to La Vergne.

The shipment from Spence moved via "SP-Ogden-U.P." to Twin Falls. A shipment from Irvine "originated on AT&SF and moved via San Bernardino, Calif., U.P.R.R.". For the out-of-line haul through Twin Falls no out-of-line charge was provided. The combination rates were applicable.

The complainants point out that the Southern Pacific and Union Pacific have an interchange point at Wells, Nev., which is south and somewhat west of Twin Falls, and contend that there is justification for routes from origins on the lines of the Southern Pacific to Wells, thence Union Pacific through Twin Falls to eastern points. The tariff naming the through rates on beans, peas and seeds from California points on the Southern Pacific, with the exception of certain points not here pertinent, provided and provide for application over routes embracing the Union Pacific with inter-

Exhibit "A"—(Continued)

change at Colton, Calif., Ogden or Portland, Oreg.

Distances from Sacramento, Calif., through Twin Falls to Kansas City, Mo., over routes requiring interchange between the Southern Pacific and Union Pacific at Wells, Ogden, and Portland are shown by the complainant to be 1990.7, 2293.5 and 2663.6 miles, respectively. Twin Falls is not an intermediate point on the established through routes. Distances over the through commodity-tariff routes from Ventura to Omaha are shown by the defendants to be 1,877, 2,141 and 2,867 miles via the Colton, Ogden and Portland interchange routes, respectively. On none of these routes is Twin Falls an intermediate point. The distance over the route through Wells and Twin Falls, sought by complainants, is shown to be 2,275 miles between the same points. The defendants explain that the Portland route was established to meet competition with the Northern Pacific Railway Company, which also interchanges traffic with the Southern Pacific at Portland.

One of the complainants' witnesses in rebuttal testimony, disagreed with mileage evidence of defendants for the reason that the aggregate distances shown failed to include the miles into and out of Twin Falls and submitted adjusted figures including such out-of-line movements. The defendants filed a motion to strike this testimony although the comparison presented by complainants' revisions is repetitious in that it is similar to the original comparison of the routes from Sacramento to

Exhibit "A"—(Continued)

Kansas City, shown above, it is nevertheless material which may properly be included in a rebuttal statement. The motion to strike this evidence is overruled.

It is contended by the complainants that service over the route through Wells, as compared with the Portland route, would be better and more economical. Average car-miles per day for all class I railroads and for one of complainants' shipments over the Portland route are divided into the distance to Twin Falls, in order to determine the number of days that would be saved by movement through Wells. Distance is not the only factor to be considered in the determination of time saved. The volume of main-line traffic is shown to be many times the volume of traffic on the Wells branch. The complainants attempted to show the number of carloads of seeds handled at Twin Falls over an extended period without a showing of the number that might have advantageously been moved if the desired route through Wells had been available. A motion by the defendants to strike this new evidence and other new evidence in the complainants' reply is granted.

The distance from Wells to Granger, over the Wells branch through Twin Falls is 454.7 miles which is 133.5 miles longer than the direct route from Wells to Granger through Ogden. From Wells via Ogden to and through Twin Falls, with the back-haul, and on to Granger the distance is 758 miles which is 304.3 miles longer than the dis-

Exhibit "A"—(Continued)

tance from Wells to Granger over the Wells branch through Twin Falls.

The position is taken by the Union Pacific that difficult and costly operations on the Wells branch warrant non-use thereof for the transportation through Twin Falls of the traffic transited at that point. From Wells to Minidoka, 58.9 miles beyond Twin Falls, there are 38.3 miles of curved track with a total curvature of 4,640 degrees, equivalent to one complete circle for each 14.16 miles of track, there are ascending and descending grades exceeding 0.5 per cent on 110 miles of track, there is frequent need for additional diesel units obtained from Pocatello, Idaho, snow drifts in cuts during the winter ranged up to 20 feet deep which required a work train with a rotary plow, and snow plows placed on the front of engines make it necessary to reduce the number of cars per engine that ordinarily can be moved. It is not shown that the unusual costs entailed result in a greater total to Granger than the cost of transporting traffic 304.3 additional miles over the back-haul route through Ogden which includes the costly operation between Minidoka and Twin Falls. As hereinbefore indicated, the route from Sacramento through Portland is 672.9 miles longer than the route via Wells and Twin Falls.

Of the 14 claims involved in these proceedings, only 2 including commodities which moved inbound to Twin Falls from origins in California. The treatment accorded the California shipments is ex-

Exhibit "A"—(Continued)

actly the same as that rendered shipments moving inbound from points in Oregon, Washington, and Idaho. Under the circumstances presented in these proceedings we are not disposed to open a route embracing the Wells Branch.

The complainants' manager at Twin Falls testified that he personally handled all shipping transactions; that his office was not furnished a copy of the transit tariff for guidance until January 18, 1954. The nine claims paid by defendants were dated April 15, 1953. No one indicated that the claim procedure was not applicable during the eight-month period before December 15, 1953. Departure from the rules and regulations of the published tariff were not justified even though the claim procedure may have been approved by an agent of the defendants. The tariff provisions must be observed.

A letter from the auditor of the Union Pacific dated December 15, 1953, requesting remittance for the amounts paid on the nine claims, was made a part of the record. It was stated therein that on the shipments covered by the claims, freight bills for the movements into Twin Falls were not surrendered and the bills of lading did not show weight, point of origin or date of inbound shipments of commodities forwarded. There was no affirmative representation that inbound freight bills were surrendered at the time shipments subject to the 14 claims were reforwarded from Twin Falls.

Exhibit "A"—(Continued)

Photostats of the outbound bills of lading do not disclose the required inbound references.

Two bills of lading forms have been and are used by the Union Pacific at Twin Falls. Although the complainants find this confusing, it is readily apparent, upon a cursory comparison, that form 1597 is for transited shipments. On the face of the bill of lading, under "Inbound Reference", eleven lines are made available for entry of transit information. Form 1591 is for shipments originated at Twin Falls and was used for all outbound shipments covered by the claims. Form 1597 was used for the complainants' shipments as early as 1944 and is currently being so used. Selection of the forms appears to have been consistent with the objective and intentions of the complainants.

Each form comes in a packet with sheets of carbon interleaved among the various documents and copies. The original bill of lading is the top sheet in each packet and the shipping order follows the first sheet of carbon. Apparently the forms are provided to shippers for the simultaneous entry of common information. This procedure saves time and eliminates the possibility of transcription errors.

It is customary for carriers to rely upon shipping orders and representations of shippers, but in the event of inconsistencies or incompleteness an inquiry or investigation is necessary. The pertinent title in the transit tariff, titled "shipping directions", reads as follows:

Exhibit "A"—(Continued)

> The bill of lading or shipping order must have inserted thereon the weight, point of origin and date of each inbound shipment covering the commodities forwarded.

It is proper and reasonable to make compliance with this rule a condition precedent to the application of the single-factor rate. Information otherwise given to, or actual knowledge by, the carrier's agent does not excuse shippers from compliance with this rule. No defects in the bills of lading issued are referred to, except the omission of inbound references, which it was incumbent upon the complainants to furnish. The complainants contend that the carriers are responsible for preparation of bills of lading, and that the Union Pacific had notice that transit privileges were desired and should have requested the inbound data and documents. Shippers are charged with knowledge of, and have the duty to comply with tariff provisions even though they be misled by the carriers as to the requirements thereof.

Attention is invited by the complainants to the report of division 3 in Southern Cotton Oil Co. vs. Atlanta, B.&C. R. Co., 270 I.C.C. 777. The applicable transit tariff therein made the claim procedure available, but required that the shipper endorse on the outbound bills of lading that transit privileges have been accorded and claim will be filed. Inadvertently the endorsements were not made. Upon the particular facts of record in that proceeding the applicable combinations were found

Exhibit "A"—(Continued)

unreasonable to the extent they exceeded corresponding joint rates with transit. The endorsement provision was subsequently canceled as unnecessary. The importance of the freight rates under control governed by regulations of the Commodity Credit Corporation and Office of Price Administration was a consideration and furthermore, in a special-docket application (which had been denied) the defendants admitted that their agent contributed to the complainants' inadvertence by failure to call attention to the omissions.

That the Commission would be warranted in granting defendant permission to waive collection of undercharges in this proceeding is further demonstrated, say complainants, by statements made in Hygrade Food Products Corp. v. Baltimore & O. R.R. Co., 292 I.C.C. 638, 641. Two transit origins were eliminated in the revision of a tariff item. The evidence indicated that the elimination was unintentional and the origins were later restored. Several proceedings were cited therein where on similar facts, the failure to provide transit during such intervals was found to be an unreasonable practice. It was observed that "the Commission does not look with favor upon the retroactive application of transit privileges, except where the showing made warrants a finding of unreasonableness of the charges assailed." The applicable rates were found unjust and unreasonable, but it was also noted that the defendants therein had failed to call attention to routing inconsisten-

Exhibit "A"—(Continued)

cies in the bills of lading. The shipper routing was impossible of execution under the transit tariff and the bills of lading contained a notation "in transit for processing."

In this proceeding, the omissions of essential information were not inadvertent.

Transit arrangements historically have been a source of discrimination. Uniform rules and regulations in effective tariffs, are a necessary step in affording equal opportunities to all shippers operating under like circumstance. Constant policing by the carriers is necessary to prevent abuses of the privileges. The rules and regulations assailed have been in effect over a long period of time at many transit points. It may be assumed that they have played an essential part in the maintenance of equality of charges for competing transit operators.

On the question of the establishment of a tariff provision which will in the future enable transit operators to conceal origin points on outbound bills and secure the benefit of through rates, one of the complainants' witnesses testified generally that shippers of grain and grain products are protected in this respect where reshipping and proportional rates are maintained. Such rates are maintained only in special circumstances. Obviously, the desired claim procedure offers opportunities for irregularities which are minimized by the established transit rules. It would impose greater administrative obligations on the defendants in policing transit

Exhibit "A"—(Continued)

arrangements and making repayments based on the through single-factor rates, and has no sound evidentiary support.

We find that the assailed rates and charges are not shown to have been or to be inapplicable, unjust or unreasonable.

We further find that because of the difficult operating conditions on the line of the Union Pacific north of Wells, routes embracing this line, as sought, are impracticable for the transportation of the traffic from California origins to destinations east of Granger, and that the established routes via Portland, maintained for the transportation thereof are not unreasonably long.

An order dismissing the complaints will be entered.

Murphy, Commissioner, dissenting in part:

The complainants, California shippers of seeds, are seeking a shorter, more reasonable route over which stoppage in transit at Twin Falls, Idaho, will continue to be available. It is their thesis that the present route via the interchange point of Portland, Oreg., with a transit stop available at Twin Falls, is unreasonably long. From Sacramento, Calif., for example, a route 672.9 miles shorter is possible if interchange of such traffic were arranged by the Southern Pacific with the Union Pacific at Wells, Nev.

No issue has been raised by the defendants as to the adequacy of the interchange facilities at

Exhibit "A"—(Continued)

Wells. The complainant refers to the Railway Equipment Register to show that Wells is a junction where traffic can be interchanged without transfer of lading. This, the defendants do not deny. Moreover, an inspection of the tariffs indicates that for some kinds of traffic, not transcontinental traffic, routes via Wells are maintained.

The only real question before us is whether the sought route is practicable. The defense urges that the route via Wells is not a practicable transcontinental route because of curves, grades, and weather on the line north of Wells. Conceding the costliness and difficulty involved in operating through this mountainous terrain, it is likewise true that equivalent costs and operating difficulties are encountered over the present route, involving as it does movement off the main line from Minidoka, Idaho, for stoppage in transit at Twin Falls, and backhaul therefrom.

In the circumstances the sought route appears to be every bit as practicable as the present routes. With reference to the existing routes, the Southern Pacific distances to Portland are somewhat shorter than to Wells, but via the sought route, the distance over the Union Pacific from Wells would be hundreds of miles shorter than the distance from Portland and would involve no backhaul. Consequently by reason of greater efficiency and economy of operation a commensurately greater profit should result to the Union Pacific as its share of the joint through rate than it now receives from

Exhibit "A"—(Continued)

traffic hauled via Portland hundreds additional miles out of the way.

Balancing advantages against disadvantages, it seems to me that the sought route is practicable, that the defendants' cost of operation and operating revenues thereover could reasonably be expected to improve, and that the complainants would be greatly convenienced if the sought route were utilized. On this record the sought route through Wells with transit stop at Twin Falls should be found desirable in the public interest and needed to provide adequate, more economic, transportation service.

ORDER

At a Session of the Interstate Commerce Commission, Division 2, held at its office in Washington, D. C., on the 27th day of March, A.D. 1956. No. 31639. Corneli Seed Company, et al., vs. Atlantic Coast Line Railroad Company, et al.

No. 31639 (Sub-No. 1)

These proceedings being at issue upon complaint and answers on file, and having been duly heard and submitted by the parties, and full investigation of the matters and things involved having been made, and said division having, on the date hereof, made and filed a report containing its findings of fact and conclusions thereon, which report is hereby referred to and made a part hereof:

Exhibit "A"—(Continued)

It is ordered, That the complaints in these proceedings be, and they are hereby, dismissed.

By the Commission, division 2.

[Seal] HAROLD D. McCOY,
Secretary.

[Endorsed]: Filed February 18, 1958.

[Title of District Court and Cause.]

MINUTE ENTRY

February 18, 1958

(Judge Taylor)

Oral argument having been waived in this case, it is ordered that the matter be submitted on briefs, plaintiff to have 15 days from today to file opening brief, defendant 15 days following to answer, and plaintiff the following 10 days to reply.

[Title of District Court and Cause.]

MEMORANDUM OPINION

This action was commenced January 19, 1955, by the plaintiff, Union Pacific Railroad Company, a Utah corporation, to recover the sum of $3,433.50, with interest from July 2, 1953. There is no dispute that $127.74 of this amount is due and owing

the plaintiff The remaining sum of $3,315.76 was paid to the defendant, Corneli Seed Co., Inc., an Idaho corporation, by the plaintiff upon claims made by the defendant for alleged overcharges made on nine (9) carloads of beans, peas, and shelled corn shipped from Twin Falls, Idaho.

Since proceedings were being instituted by the defendant before the Interstate Commerce Commission to determine the applicability of the tariff provisions upon which the instant action is based as applied to fourteen (14) shipments (of which the nine (9) shipments here involved were a part), it was stipulated that the defendant's time to answer would be extended until twenty (20) days after the decision of the Interstate Commerce Commission was rendered. The Interstate Commerce Commission made its decision and thereafter the defendant answered. The matter has now been submitted to the Court on an agreed Statement of Facts.

From the agreed Statement of Facts it appears that the nine (9) carloads of beans, peas, and corn were shipped from points of origin in California, Oregon, and Washington, to a transit station at Twin Falls, Idaho, where the seeds were stopped for processing. After processing the seeds were shipped on to their final destination.

It is stated in the agreed Statement of Facts that:

"That the rules and regulations of the transit tariff of the plaintiff applicable to the shipments involved herein provided that when shipments are

forwarded from the transit station, in this case Twin Falls, Idaho, unexpired inbound freight bills which had been recorded, or tonnage credit slips must be surrendered and cancelled; that the outbound bills of lading or shipping orders must have inserted thereon the weight, point of origin, and date of each inbound shipment covering the commodities forwarded and that the transit rate would not apply if shippers fail or decline to comply with all such rules and regulations; * * *"

The defendant had complied with the tariff rules and regulations, set out in substance above, for several years during and subsequent to 1944, and received the benefit of the transit or single-factor rate. By use of the information contained on the outbound bill of lading the defendant's customers began dealing directly with the defendant's sources of supply with a resultant loss of business to the defendant. To stop this loss the defendant's local representative adopted the practice of making shipments out of the transit point (Twin Falls) by using the regular forms of bills of lading used for shipments not entitled to transit privileges. These bills of lading did not show the information previously shown in compliance with the transit tariff rules and regulations. Then to secure the transit rate the defendant's representative filed with the plaintiff overcharge claims, attaching thereto copies of the bill of lading for the outbound shipment, a memorandum bill marked "for transit consideration only", which contained inbound references, and a statement showing a computation of the differ-

ence between the transit rate and the combination rate. Pursuant to this practice claims were paid by the plaintiff, through and including the claims made on the nine (9) shipments for which the plaintiff seeks recovery. Thereafter the practice was stopped and the instant action commenced to recover the amounts paid to defendant on its claims for alleged overcharges on the nine (9) shipments here in question.

In its report and order dismissing the defendant's complaint the Interstate Commerce Commission found, in effect, that the procedure followed by the defendant was not in compliance with the tariff rules and regulations relating to transit privileges; that the procedure specified by the tariff rules and regulations had to be observed before the defendant was entitled to transit privileges. It was found in the said report that, "It is proper and reasonable to make compliance with this rule a condition precedent to the application of the single-factor rate."

Duly filed tariffs bind both carrier and shipper with the force of law. Lowden v. Simonds-Shields-Lonsdale Grain Co., 59 S. Ct. 612; 306 U. S. 516. The shipper is conclusively presumed to know the proper tariff rates. Pettibone v. Richardson, 7 Cir., 126 F. 2d 969. No estoppel can arise against the carrier nor can a waiver be made by the carrier to prevent the collection of the applicable tariff rate; and law requires the railroad to charge and collect the applicable rates. Davis v. Henderson, 45 S. Ct. 24, 266 U. S. 92; Pittsburgh, C., C.&St.L.

Ry. Co. v. Fink, 40 S. Ct. 27, 250 U.S. 577; West Coast Products Corp. v. Southern Pacific Co., 9 Cir., 226 F. 2d 830.

These matters of law do not appear to be contested by the parties. It is apparently the contention of the defendant that the procedure followed in regard to the shipping of the nine (9) carloads of seed was such a substantial compliance with the tariff rules and regulations here involved as to entitle the defendant to the single-factor or transit rate; and that the Court can determine this question as a matter of law.

Assuming, without deciding, that this Court is not bound by the Interstate Commerce Commission's determination, never the less, this Court is in agreement.

In Chicago & N. W. R. R. Co. v. Connor Lumber & Land Co., 7 Cir., 212 F. 2d 712, 717, it is stated:

"It appears that, as to all inbound shipments involved herein, defendant originally desired to and did avail itself of the transit rates plan set up by the aforesaid tariff. It thereby became obligated, in order to obtain the concession of such lower through rates to comply with every pertinent provision of the tariff imposing duties upon it as a shipper."

The Interstate Commerce Commission has held that the tariff rules and regulations here involved to be reasonable and proper. The language of the said tariff rules and regulations is specific and mandatory as to what must be done by the shipper

in order to secure the single-factor or transit rate. These things were not done by the defendant.

It appears from the report of the Interstate Commerce Commission that the difference between the procedure followed by the defendant in regard to the nine (9) carloads of seed here involved and that specified in the tariff rules and regulations amounts to more than a mere matter of form. It is stated on page 12 of the Interstate Commerce Commission Report and Order that:

"Transit arrangements historically have been a source of discrimination. Uniform rules and regulations in effective tariffs, are a necessary step in affording equal opportunities to all shippers operating under like circumstance. Constant policing by the carriers is necessary to prevent abuses of the privileges. The rules and regulations assailed have been in effect over a long period of time at many transit points. It may be assumed that they have played an essential part in the maintenance of equality of charges for competing transit operators."

Again on page 12 it is stated:

"Obviously, the desired claim procedure offers opportunities for irregularities which are minimized by the established transit rules."

Accordingly, it is the conclusion of the Court that the procedure followed by the defendant in shipping the nine (9) carloads of beans, peas, and shelled corn was not a compliance with the terms of the tariff regulations so as to entitle the defendant to transit privileges.

Plaintiff is therefore entitled to judgment against defendant for the sum of $3,433.50, together with interest thereon from July 2, 1953, to the date of judgment herein.

Dated this 11th day of April, 1958.

/s/ FRED M. TAYLOR,
U. S. District Judge.

[Endorsed]: Filed April 11, 1958.

In The United States District Court for the District of Idaho, Southern Division

No. 3148

UNION PACIFIC RAILROAD COMPANY, a corporation, Plaintiff,

vs.

CORNELI SEED COMPANY, INC., a corporation, Defendant.

JUDGMENT

This cause having been heretofore submitted to the Court upon an Agreed Statement of Facts with Briefs of the parties, Findings of Fact being waived, and the same having been considered and it appearing that the issues herein should be found for the plaintiff and that it should have judgment as demanded in its complaint, being in the sum of Three Thousand Four Hundred Forty-three and 50/100ths Dollars ($3,443.50), with interest at 6% from July 2nd, 1953.

It Is Therefore Ordered and Adjudged that the plaintiff, Union Pacific Railroad Company, have and recover of and from the defendant, Corneli Seed Company, Inc., the sum of $3,443.50 principal, and the sum of $990.58 as interest, or a total sum of $4,434.08, plus costs taxed in the amount of $37.00, with interest on said judgment at the rate of 6% per annum, and that plaintiff have execution therefor.

Dated, April 14th, 1958.

/s/ FRED M. TAYLOR,
District Judge.

Entered: April 14, 1958.

[Endorsed]: Filed April 14, 1958.

[Title of District Court and Cause.]

MEMORANDUM OF COSTS AND DISBURSEMENTS

Clerk's Fee	$15.00
Marshal's Costs	2.00
Attorney's Docket Fee	20.00
	$37.00

State of Idaho,
County of Bannock—ss.

Costs taxed this 21st day of April, 1958, in the amount of $37.00.

L. H. Anderson, being first duly sworn, deposes and says:

That he is one of the attorneys for the Plaintiff, Union Pacific Railroad Company, in the above entitled action, and as such is better informed relative to the above costs and disbursements than the said plaintiff; that to the best of his knowledge and belief the items in the above Memorandum contained are correct, and that said disbursements have been necessarily incurred in said action.

/s/ L. H. ANDERSON,

Subscribed and sworn to before me this 15th day of April, 1958.

[Seal] /s/ ROSA ENKE,
Notary Public for Idaho, Residing at: Pocatello, Idaho.

[Endorsed]: Filed April 15, 1958.

[Title of District Court and Cause.]

NOTICE TO TAX COSTS

To: Ralph R. Breshears and Greensfelder, Hemker & Wiese, Attorneys for the Above Named Defendant:

Please Take Notice that Plaintiff's Memorandum of Costs filed herein April 15, 1958, a copy of which is attached hereto, will be presented to the Clerk of the above entitled Court for taxation, at his office in the Federal Building, in the City of Boise, Idaho, on the 21st day of April, 1958, at ten o'clock

in the forenoon of that day.

Dated, April 15, 1958.

/s/ BRYAN P. LEVERICH,
/s/ L. H. ANDERSON,
/s/ E. C. PHOENIX,
/s/ D. A. BYBEE,
Attorneys for Plaintiff.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed April 15, 1958.

[Title of District Court and Cause.]

DEFENDANT'S MOTION FOR NEW TRIAL AND TO AMEND JUDGMENT ENTERED APRIL 14, 1958

Comes now the defendant in the above cause within ten days of April 14, 1958, the date of entry of judgment in this cause, and moves the Court to grant unto defendant a new trial herein and to amend the judgment herein entered April 14, 1958, by striking from the first paragraph thereof the following:

> "in the sum of Three Thousand Four Hundred Forty-three and 50/100ths Dollars ($3,443.50), with interest at 6% from July 2nd, 1953."

and inserting in lieu thereof:

> "in the sum of $127.74 with interest at 6% from July 2, 1953"

and by striking from the second paragraph thereof the following:

> "the sum of $3,443.50 principal, and the sum of $990.58 as interest, or a total sum of $4,434.08, plus costs taxed in the amount of $....."

and inserting in lieu thereof the following:

> "the sum of $127.74 principal and the sum of $36.64 as interest or a total sum of $164.38 plus costs taxed in the amount of $....."

for the following reasons:

1. Under the Agreed Statement of Facts, the judgment in favor of plaintiff is erroneous as a matter of law and should have been in favor of defendant.

2. The Court erroneously misconstrued and misapplied statements of fact and ignored statements of fact contained in the agreed statement of facts.

3. The Court erroneously failed to hold as a matter of law that defendant complied with the tariff provisions in question and that plaintiff was entitled to the benefit of the transit tariff on the shipments in question.

4. The Court erroneously concluded that the procedure followed by defendant was not a compliance with the terms of the tariff regulations in question so as to entitle defendant to transit privileges.

5. The Court erroneously followed the determination of the Interstate Commerce Commission.

6. The findings contained in the memorandum

opinion of the Court and the judgment are erroneous as a matter of law under the record in this cause.

Wherefore, defendant prays that defendant be granted a new trial herein and that the judgment herein be amended in the respects hereinabove set out.

GREENSFELDER, HEMKER
& WIESE,
/s/ By EDWARD L. WIESE,
/s/ RALPH R. BRESHEARS,
Attorneys for Defendant.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed April 22, 1958.

[Title of District Court and Cause.]

STIPULATION

It Is Hereby Stipulated, by and between the parties hereto through their respective counsel, that Defendant's Motion for New Trial and to Amend Judgment Entered April 14, 1958, heretofore filed herein, be submitted on briefs and that the plaintiff in the above-entitled case may have until May 6th, 1958, in which to file a reply to the memorandum in support of defendant's motion, which memorandum has been filed, and that the defendant may have fifteen days from and after the date of receipt of a

copy of said reply memorandum in which to reply to said reply memorandum.

Dated this 28th day of April, 1958.

/s/ BRYAN P. LEVERICH,
/s/ L. H. ANDERSON,
/s/ E. C. PHOENIX,
Attorneys for Plaintiff.

GREENSFELDER, HEMKER & WIESE,
/s/ By EDWARD L. WIESE,
/s/ RALPH R. BRESHEARS,
Attorneys for Defendant.

ORDER

Upon reading the above stipulation, good cause appearing therefor, It Is Ordered that Defendant's Motion for New Trial and to Amend Judgment Entered April 14, 1958, be submitted on briefs, that the plaintiff have until May 6th, 1958, to file a memorandum or reply to the memorandum in support of Defendant's Motion for New Trial and to Amend Judgment, and that defendant have fifteen days from and after receipt of a copy of plaintiff's reply memorandum or brief in which to reply thereto.

Dated this May 29th, 1958.

/s/ FRED M. TAYLOR,
District Judge.

[Endorsed]: Filed April 29, 1958.

[Title of District Court and Cause.]

ORDER

This case was submitted to the Court on an agreed statement of facts. In its memorandum opinion filed on April 11, 1958, the Court found for the plaintiff, Union Pacific Railroad, and on April 14, 1958, judgment was entered. On April 22, 1958, the defendant, Corneli Seed Co., Inc., filed a "Motion for New Trial and to Amend Judgment Entered April 14, 1958." This motion, by stipulation of counsel, was submitted to the Court on briefs.

After a consideration of defendant's Motion and the briefs of counsel, it is this Court's conclusion that the original opinion and judgment are correct.

Accordingly, it is Ordered that defendant's motion be, and the same is hereby denied.

Dated this 2nd day of June, 1958, at Pocatello, Idaho.

/s/ FRED M. TAYLOR,
United States District Judge.

[Endorsed]: Filed June 2, 1958.

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice is hereby given that defendant, Corneli Seed Company, Inc. hereby appeals to the United States Court of Appeals for the Ninth Circuit from the judgment in this cause entered on April 14,

1958, in the United States District Court for the District of Idaho, Southern Division. A motion for new trial and to amend said judgment was timely filed April 22, 1958, and by order entered June 2, 1958 denied. This appeal is taken within thirty days after the denial of said motion in compliance with Federal Rule 73.

CORNELI SEED COMPANY, INC.,
Appellant,
/s/ By EDWARD L. WIESE,
/s/ FORREST M. HEMKER,
Attorneys for Appellant.

[Endorsed]: Filed June 25, 1958.

[Title of District Court and Cause.]

APPEAL BOND

Know all men by these presents, that we, Corneli Seed Company, Inc., as principal, and Hartford Accident and Indemnity Company, a corporation, of Hartford, Connecticut, as surety, are held and firmly bound unto Union Pacific Railroad Company in the sum of $5,000, for the payment of which, well and truly to be made, we bind ourselves, our heirs, executors, administrators, and successors, jointly and severally, firmly by these presents.

The condition of the above obligation is such that whereas Union Pacific Railroad Company has in the United States District Court for the District of

Idaho, Southern Division, in the above-entitled cause therein pending recovered a judgment against the said Corneli Seed Company, Inc.; and whereas the above-named appellant has according to law, taken an appeal from the said judgment.

Now, Therefore, if the said appellant shall satisfy the said judgment in full together with costs, interest and damages for delay, if for any reason the appeal is dismissed or if the judgment is affirmed and satisfy in full such modification of the judgment and such costs, interest and damages as the appellate court may adjudge and award, or if the said judgment be set aside, then this obligation shall be void; otherwise to remain in full force and effect.

Sealed with our seals and dated at St. Louis, Missouri, this 20th day of June, 1958.

[Seal] CORNELI SEED COMPANY, INC., a corporation,
/s/ By EDWARD PAGE, Pres., Principal.

[Seal] HARTFORD ACCIDENT AND INDEMNITY COMPANY, a corporation,
/s/ By JOSEPH M. O'DAY, Surety.

Approved: June 26, 1958.

/s/ FRED M. TAYLOR,
U. S. District Judge.

State of Missouri,
City of St. Louis—ss.

I, Carl A. J. Miller, a Notary Public in and for the said City, in the State aforesaid, do hereby certify that Joseph M. O'Day, who is personally known to me to be the same person who signed the above and foregoing instrument as the Attorney-in-Fact for the Hartford Accident and Indemnity Company, appeared before me this day in person and acknowledged that he signed the name of the Hartford Accident and Indemnity Company thereto, as his Principal, and his own name as Attorney-in-Fact as the free and voluntary act of his said Principal for the uses and purposes therein set forth, and that he executed the said instrument under authority given him by his said Principal.

Given under my hand and Notarial seal, this 20th day of June, A. D. 1958.

[Seal] /s/ CARL A. J. MILLER,
Notary for the County of St. Louis which adjoins the City of St. Louis. My commission expires June 11, 1959.

Power of Attorney Attached.

[Endorsed]: Filed June 25, 1958.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

United States of America,
District of Idaho—ss.

I, Ed. M. Bryan, Clerk of the United States District Court for the District of Idaho, do hereby certify that the foregoing papers are that portion of the original files designated by the parties and as are necessary to the appeal under Rule 75 (RCP):

1. Complaint
2. Summons with return thereon
3. Stipulation and order re: defendant to plead
4. Answer of defendant
5. Agreed statement of facts, with Exhibit A attached
6. Minutes of the court of February 18, 1958
7. Defendant's interrogatories to plaintiff
8. Memorandum Opinion
9. Judgment (Entered April 14, 1958)
10. Memorandum of costs and disbursements
11. Notice to tax costs
12. Defendant's motion for new trial and to amend judgment
13. Stipulation and order to submit motion for new trial and to amend judgment on briefs
14. Order denying motion for new trial and to amend judgment
15. Notice of appeal
16. Appeal bond
17. Designation of contents of record on appeal.

In Witness Whereof I have hereunto set my hand and affixed the seal of said court this 11th day of July, 1958.

[Seal] ED. M. BRYAN,
Clerk,

/s/ By LONA MANSER,
Deputy.

[Endorsed]: No. 16108. United States Court of Appeals for the Ninth Circuit. Corneli Seed Company, a corporation, Appellant, vs. Union Pacific Railroad Company, a corporation, Appellee. Transcript of Record. Appeal from the United States District Court for the District of Idaho, Southern Division.

Filed: July 14, 1958.

Docketed: July 22, 1958.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 16108

CORNELI SEED COMPANY, INC., a corporation, Appellant (Defendant).

vs.

UNION PACIFIC RAILROAD COMPANY, a corporation, Appellee (Plaintiff),

APPELLANT'S POINTS TO BE RELIED UPON

Appellee, Union Pacific Railroad Company, brought this action against appellant, Corneli Seed Company, Inc., to recover freight transportation charges allegedly due appellee by reason of its having granted Corneli the through rate freight charges, on the theory that notwithstanding the shipments involved qualified for the through rate, that Corneli was not entitled to same because of its alleged failure to comply with the terms of the transit tariff in failing to make certain notations on bills of lading. Appellant Corneli asserted that there had been a compliance with the terms of the tariff covering the shipments involved in this case.

On an agreed statement of facts, the District Court for the District of Idaho, Southern Division, entered judgment for the appellee, Union Pacific Railroad Company, against the appellant, Corneli Seed Company, Inc. in the amount of $3,443.50

principal and $990.58 interest, a total of $4,434.08 plus costs with interest to run at 6% until satisfaction.

Points on which the appellant intends to rely are as follows:

1. The Court erred in entering judgment for the appellee for as a matter of law under the Agreed Statement of Facts, it appears that the appellant has complied with the transit tariff.

2. The Court erred in holding that the appellant was not entitled to the benefit of the transit tariff for under the law, exact, technical, literal compliance with the terms of transit tariffs is not required where such a compliance leads to an unjust or absurd result. The compliance in this case was sufficient where the shipper, appellant, was and is clearly entitled to the benefit of the through rate, in view of the lack of any discrimination and that the shipments were in truth and in fact transit shipments.

3. The Court erred in misconstruing and misapplying the agreed statement of facts and the judgment in favor of the appellee is erroneous as a matter of law.

4. The Court erred in failing to hold as a matter of law that the appellant complied with the tariff provisions in question and that appellant was entitled to the benefit of the transit tariff on the shipments in question.

5. The Court erred in concluding that the procedure followed by appellant was not in compliance

with the terms of the tariff regulation in question so as to entitle appellant to transit privileges.

6. The Court erred in following the determination of the Interstate Commerce Commission.

7. The Court erred in overruling the appellant's motion for new trial and to amend judgment.

CORNELI SEED COMPANY, INC.,
Appellant,
/s/ By EDWARD L. WIESE,
/s/ FORREST M. HEMKER,
Attorneys for Appellant.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed July 25, 1958. Paul P. O'Brien, Clerk.

[Title of Court of Appeals and Cause.]

DESIGNATION OF CONTENTS OF RECORD TO BE PRINTED UNDER THE SUPERVISION OF THE CLERK

Now comes the appellant, defendant, Corneli Seed Company, Inc., and hereby designates for printing under the supervision of the Clerk of this Court, the complete record herein filed including the pleadings, the agreed statement of facts and Exhibit "A" attached thereto; the Memorandum Opinion of the District Court of April 11, 1958, the Judgment of the District Court on April 14, 1958, Appellant's (Defendant's) Motion for a New Trial and to

Amend Judgment filed April 22, 1958, Order of the District Court of June 2, 1958, denying said Motion, Appellant's (Defendant's) Notice of Appeal, Appeal Bond, Order Approving Appeal Bond, this Designation Respecting the Printed Record, the Appellant's Points to be Relied Upon, the transcript of all docket entries and any other items comprising the complete record as filed in this Court. Appellant, defendant deems the complete record material to the consideration of this appeal.

CORNELI SEED COMPANY, INC.,
Appellant,

/s/ By EDWARD L. WIESE,
/s/ FORREST M. HEMKER,
Attorneys for Appellant.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed July 25, 1958. Paul P. O'Brien, Clerk.

No. 16,108.

IN THE

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT.

CORNELI SEED COMPANY,
Appellant,

vs.

UNION PACIFIC RAILROAD COMPANY,
Appellee.

Appeal from the United States District Court for the District of Idaho, Southern Division.

OPENING BRIEF OF APPELLANT.

FORREST M. HEMKER,
GREENSFELDER, HEMKER & WIESE,
705 Olive Street,
St. Louis 1, Missouri,
Attorneys for Corneli Seed Company, Appellant.

St. Louis Law Printing Co., Inc., 415 N. Eighth Street. CEntral 1-4477.

FILED
SEP 25 1958

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No. 16,108.

IN THE

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT.

CORNELI SEED COMPANY,
Appellant,

vs.

UNION PACIFIC RAILROAD COMPANY,
Appellee.

Appeal from the United States District Court for the District of Idaho, Southern Division.

OPENING BRIEF OF APPELLANT.

JURISDICTION.

This action was brought by the Union Pacific Railroad Company, appellee, as a common carrier under the Interstate Commerce Act, 49 U. S. C. A., Section 6, against the Corneli Seed Company, appellant, a shipper, for freight due for alleged undercharges claimed to arise from the application and allowance of transit rates from points of

origin to ultimate destinations for transit shipments instead of the combined local rates from point of origin to the transit point and from the transit point to ultimate destination.

The case was submitted on an agreed statement of facts to the United States District Court for the District of Idaho, Southern Division (R. 14). Jurisdiction of the District Court was based on Title 28, U. S. C. A., Section 1337 and Title 28, U. S. C. A., Section 1332 (R. 14).

From a decision and judgment of the District Court in favor of plaintiff, appellee herein, in the amount of $3,443.50 with interest at 6% from July 2, 1953, the defendant, appellant herein, has appealed.

This court has jurisdiction to review the judgment under the United States Judicial Code. Title 28, U. S. C. A. 1291 and Title 28, U. S. C. A. 1294.

STATEMENT OF FACTS.

This cause was submitted to the District Court under an agreed statement of facts, hence appellant deems it unnecessary to review the pleadings in detail (R. 14). The stipulation of facts shows the following:

Appellant, Corneli Seed Company, since at least January 5, 1944, and up to and including December 15, 1953, was engaged in the business of processing and wholesaling various seeds, and in the course of said business Corneli purchased seeds in carload lots from various growers, producers and processors at points in California, Idaho, Oregon and Washington, and shipped such seeds from points of origin over appellee's route to Twin Falls, Idaho, a specified transit point, where they were stopped in transit for processing and and then subsequently forwarded to destinations in other states (R. 14, 15).

A through or single factor rate was available to Corneli for said shipments under the terms of Union Pacific's transit tariff then in force, Twin Falls, Idaho being a designated transit point. Such transit tariff provided for a lesser rate than the combination of rates from points of origin to Twin Falls, Idaho, and from Twin Falls to final destinations (R. 15).

Among the numerous various rules and regulations of the transit tariff then in force relating to shipments from Twin Falls to eastern destinations it was provided that:

> "The bill of lading or shipping order must have inserted thereon the weight, point of origin and date of each inbound shipment covering the commodities forwarded."
>
> (R. 35, 36, 15)

From January 5, 1944 up to and including January or February, 1949, Corneli indicated the so-called "inbound" references, that is, point of origin, weight and commodity on standard forms of outbound bills of lading for transit shipments from Twin Falls to ultimate destinations. The through transit rate was applied and paid, credit being taken for the amount of the inbound freight previously paid for the shipment into the Twin Falls transit point at local rates (R. 14, 15).

It was ascertained that customers of Corneli were learning from said outbound bills of lading, which showed the point of origin, the identity of Corneli's producers and sources of supply and were purchasing directly from them. In order to effect discontinuance of this practice by Corneli's customers, beginning in January or February 1949 Corneli adopted, and Union Pacific concurred in, the following procedures respecting the application of through transit rates to Corneli's transit shipments: Corneli used Union Pacific's form of bill of lading for non-transit out-

bound shipments and paid the applicable rate from Twin Falls to ultimate destinations rather than the single factor transit rate from point of origin, although it was understood by the parties that such shipments were to receive transit rates. This form of bill of lading did not call for inbound data. Corneli then shortly after filed a claim for the application of the through single factor transit rate, supporting same by the original inbound freight bill which contained inbound references, that is, weights and point of origin and date which showed the transit rate was applicable (R. 16, 17). Corneli having paid the local rate into and out of Twin Falls, and the transit rate being lower than such combined rates, Union Pacific allowed and applied the transit rate and refunded the over payment to Corneli. The foregoing method of applying the through transit rate to Corneli's transit shipments continued until on or about December 15, 1953 when Union Pacific concluded that Corneli had not complied with its transit tariff by failing to show inbound data on outbound bills of lading (R. 20, 21).

This case involves the application by Union Pacific under the procedure above described of its transit rate to 9 carload lots of beans, peas or shelled corn shipped by Corneli through Twin Falls, where they were stopped in transit for cleaning and processing, during the months of February and March, 1953, and subsequently forwarded to various eastern destinations (R. 17, 18).

The claim for application of the transit rate and supporting bills of lading showing the inbound information entitling Corneli to the lower transit rate was made on April 15, 1953, and the transit rate was applied for these shipments and the overcharge refunded to Corneli. The transit rate was applied under the same procedure used and honored by Union Pacific since January or February, 1949 (R. 18, 20).

After the December 15, 1953, determination by Union Pacific that the application of the through transit rate procedure adopted did not comply with the transit tariff, Union Pacific filed this action on January 19, 1955, to recover the difference between the transit rate and the combined single local rates into and out of Twin Falls, which amount had been refunded to Corneli on its claim for application of the transit rate dated April 15, 1953, the sum involved being $3,443.50 with interest at 6% from July 2, 1953 (R. 5, 21). Corneli concedes that $127.74 of this amount is due Union Pacific by reason of a mathematical error in the application of the transit tariff (R. 19, 20).

Thereafter, on October 1, 1954, Corneli filed a complaint with the Interstate Commerce Commission challenging the applicability, reasonableness and lawfulness of the local rates respecting the shipments involved in this action and seeking Commission determination of a more reasonable route from California to Twin Falls by substituting Wells, Nevada, as an interchange point instead of Portland, Oregon.

By stipulation between the parties it was agreed that Corneli could have 20 days from which and after the decision of the Interstate Commerce Commission in which to plead to Union Pacific's complaint.

On March 27, 1956, the Interstate Commerce Commission made its report and order wherein it found that "the assailed rates and charges are not shown to have been or to be inapplicable, unjust or unreasonable", and the contention respecting the interchange point was disallowed with Commissioner Murphy dissenting (R. 39). A rehearing was denied August 30, 1956 (R. 22, 23)

The only omission in the bills of lading on outbound shipments from Twin Falls in controversy was the omission of inbound references, which information was provided on

the claim for application of the transit rates before same were applied and allowed. All 9 shipments were admittedly entitled to transit rates and were in fact transited shipments (R. 47, 48).

Thereafter, the District Court held that the procedure adopted was not a compliance with the transit tariff regulations and that Union Pacific was entitled to recover the $3,443.50 (and interest and costs paid by Union Pacific to Corneli respecting the 9 carloads of beans herein, and entered judgment accordingly.

Corneli duly filed its motion for a new trial and to amend the judgment. The motion was denied June 2, 1958. Deeming itself aggrieved by the decisions of the District Court and its failure to vacate or amend its judgment of April 14, 1958, Corneli duly prosecutes its appeal to the end that the judgment of April 14, 1958, be reversed, vacated and set aside, and appellant accorded such relief as it is entitled to under the record.

THE QUESTION PRESENTED.

The transit tariff of appellee, Union Pacific Railroad Company, provided that outbound bills of lading or shipping orders have inserted thereon inbound references showing the weight, point of origin and date of each inbound shipment covering the commodities forwarded and that the transit rate does not apply if shippers fail or decline to comply with such regulations.

Appellant, Corneli Seed Company, a shipper, and Union Pacific concurred in adopting a procedure which was pursued over four years, whereby Corneli made outbound shipments of seed admittedly entitled to the through transit rate from Twin Falls without showing on outbound bills of lading inbound references. Corneli then filed a claim

supported by the required inbound references for application of the through transit rate from point of origin to the final destination. Having previously paid the combined inbound freight from origin into and then out of Twin Falls, when Union Pacific applied the transit rate to the transit shipments, same being lower than the combined rates, it refunded the overcharge to Corneli. Deeming the transit rate to have been erroneously allowed and applied and that the higher combined local rates were applicable, Union Pacific sued Corneli for alleged undercharges of $3,443.50 and the District Court on an agreed statement of facts found for Union Pacific and against Corneli.

The question presented is whether the construction placed upon Union Pacific's transit tariff by both Union Pacific and Corneli that under the tariff transit rates were applicable to transit shipments upon the furnishing of inbound references of weight, origin and date after the date of outbound shipment was a proper construction and practice and a compliance with the tariff, or whether the furnishing of inbound references on outbound bills of lading at the date of forwarding was the only and exclusive method whereby the transit rate was applicable.

SPECIFICATION OF ERRORS.

1. Under the agreed statement of facts, the court erred as a matter of law in construing the Union Pacific transit tariff by holding that such tariff required Corneli, as a shipper, as a condition precedent to the application of a through transit rate to note at the time of shipment, inbound references on outbound bills of lading (R. 46, 47).

2. The court further erred in failing to hold that the construction of Union Pacific and Corneli that the transit rate was applicable and the tariff complied with so long as the inbound references were furnished prior to the allowance and application of the transit rate was a proper construction and a compliance with the transit tariff.

3. The foregoing errors of the court were given effect by its finding and judgment against appellant. The court erred in failing to sustain, and in denying, appellant's motion for a new trial and to amend the judgment of April 14, 1958 (R. 55) so as to find for appellant except with respect to $127.74 admittedly due appellee.

SUMMARY OF ARGUMENT.

The argument will be directed to the establishment of three propositions:

1. That the construction Union Pacific and Corneli placed upon Union Pacific's transit tariff that the tariff was complied with by the application of the transit rate to admittedly transit shipments upon receipt by Union Pacific of inbound data respecting point of origin, weight and date was a proper construction and application of the transit tariff and a compliance with the tariff. The court erred in failing to so hold.

2. That the tariff requirement that inbound references be noted on outbound bills of lading was not a mandatory condition precedent to application of transit rates to transit shipments and the court erred in failing to so hold.

3. That this case having been tried on an agreed statement of facts presents only a question of law respecting which the decisions of the District Court and of the Interstate Commerce Commission are not binding on this Court.

I.

At the outset, appellant acknowledges that, as stated by the District Court, tariffs are binding on shipper and carrier alike and it is presumed that a shipper knows the proper rates. Appellant concedes that a carrier cannot be estopped or waive the collection of applicable rates and that the law requires the carrier to charge and collect the applicable rates. These principles are well recognized and stem from the Interstate Commerce Act which prohibits discrimination and makes it a crime to give or receive rebates or preferences (R. 45, 46).

Although this court is doubtless familiar with "transit" procedures since it has had occasion to consider such matters as evidenced by its published opinions, it may be helpful to briefly describe transit operations. It is customary for all carriers to allow transit privileges, that is, a shipper may ship into a designated transit point (such as Twin Falls, Idaho, the transit point of Union Pacific involved in this case) and there unload the goods for storage or processing. The inbound bill of lading or freight bill is "recorded for transit" meaning thereby that the shipper has the privilege, usually for a year, of forwarding the same cargo to a final destination at the through transit rate from point of origin to final destination rather than the combination of the local rates which would be applicable for separate shipments into and out of the transit point. The court in Utah Poultry Producers Corp. v. Union Pacific R. Co. (10th Cir. 1945), 147 F. 2d 975, described transit privileges as follows, l. c. 976:

> "When a shipment is stopped in transit and is subsequently re-shipped to its ultimate destination, there are in fact two separate, distinct transportation services. Transit privileges rest upon the fiction that these two distinct transportations constitute a continuous shipment of an identical article from point of origin to the point of ultimate destination."

Thus, to take advantage of a transit privilege and rate the shipper must "forward" or ship outbound from the transit point identical cargo previously shipped to the transit point. Shippers such as Corneli customarily have large tonnage credits recorded for transit with carriers. As shipments are made outbound from the transit point the tonnage credit is debited by deducting the tonnage of the outbound cargo. As in this case, by the time the cargo is shipped outbound from the transit point the inbound freight has been paid. In cases where the combined rates

into and out of the transit point exceed the through transit rate the result is that there has been an overcharge for the inbound carriage and this is adjusted so as to exact only the applicable transit rate for the transit shipment.

In the case at bar, Corneli shipped 9 carloads of beans from points of origin in California, Oregon and Washington to Union Pacific's transit station at Twin Falls, Idaho, where the seeds were stopped in transit for processing and subsequently re-shipped to final destinations in Missouri, Wisconsin and Michigan (R. 17, 18). Union Pacific's transit tariff provided that there be noted on outbound bills of lading the weight, point of origin and date of the inbound shipment of the commodities forwarded (R. 15). From 1949 to 1953 the outbound bills of lading did not note inbound references, and Corneli paid freight at the combination local rates for separate shipments into and out of Twin Falls, and then claimed its transit privileges supporting its claim for allowance and application of the transit rate by supplying the inbound references. The Union Pacific thereupon allowed and applied the through transit rate and refunded the overcharge. The result was that Corneli paid the exact transit rate applicable to admittedly transit cargo (R. 17). By its action in this case Union Pacific seeks to apply the combination rates and collect on the theory it has undercharged Corneli and discriminated in its favor. Since only the lawful rate can be applied and paid, the question is which rate is lawful under the admitted facts. It is the position of Corneli that the through transit rate as applied, allowed and paid is the proper and lawful rate and that the collection in this case by Union Pacific of the combined rate would constitute the exaction of an illegal and discriminatory rate by subjecting transit cargo to the local, rather than the through, rates.

The crux of the case is whether the construction and practice mutually adopted by Union Pacific and Corneli,

whereby it was considered that the transit tariff was complied with by furnishing inbound references after shipment rather than on outbound bills of lading, was a compliance with the tariff. We submit that such is the case.

There is no suggestion of bad faith, no intimation of an attempt to grant or receive a preference or rebate or to discriminate against other shippers. The shipments were in fact transit shipments and entitled to the transit rate. The inbound references were received, examined, approved and acted upon prior to the application and allowance of the transit rate. Unquestionably, the Union Pacific was able to debit Corneli's tonnage credits and satisfy itself respecting the cargo for it actually did so over a period of over four years. Obviously, the purpose of giving Union Pacific inbound references was as fully satisfied as if same were on outbound bills of lading.

It is the law that when a carrier and a shipper place a construction upon a tariff and act in accordance therewith, such construction and practice is entitled to great weight, and it is presumed that both parties conducted their transactions in compliance with the law. For example, in Pacific Portland Cement Company v. Western Pacific Railroad Company (9th Cir. 1950), 184 F. 2d 35, this Court had before it the following situation. The Western Pacific tariff provided with respect to demurrage charges that if the shipper appropriated an empty car without ordering it, it would be considered as having been ordered and become subject to demurrage charges. The question presented was what constituted an "appropriation." Western Pacific and Pacific Portland for 20 years had construed the tariff as permitting inbound cars after same were unloaded to be stored on the tracks of Pacific Portland in its yard. Demurrage was paid from the time the cars were spotted for loading. Western Pacific claimed that since the cars were eventually returned under load that this was sufficient to establish that the cars were held for the purpose of load-

ing from the time they first entered Pacific Portland's tracks, and that they were therefore deemed to have been appropriated at that time within the meaning of the tariff. The District Court's judgment permitting recovery by Western Pacific was reversed by this Court. The opinion points out that if the appropriation took place when the cars were placed on Pacific Portland's tracks, and if Western Pacific failed to charge demurrage from such time the appropriation took place both parties were guilty of crimes, and said that in the absence of substantial evidence to the contrary it is presumed that both parties conducted their business in compliance with the law. Further, that since the demurrage was charged only from the time the cars were spotted, the court would presume that the parties understood and intended that the cars would not be considered appropriated until that time. At the conclusion of the opinion, Judge Orr, speaking for this Court, said, l. c. 39:

> "We also recognize the overriding purpose of the Interstate Commerce Act to enforce the terms of published tariffs rigorously against all carriers and shippers alike so as to prevent special concessions and discriminations in interstate railroad traffic. This policy and the purpose of the tariff would not be served by striking down as illegal the long standing, reasonable and beneficial arrangement between these parties for utilizing otherwise empty trackage owned by appellant in order to relieve congestion at an important railroad yard on an important interstate line."

On substantially similar facts, District Judge Darr reached the same conclusion in Southern Railway Company v. Aluminum Company of America (E. D. Tenn. 1951), 119 F. Supp. 389, affirmed (6th Cir. 1954), 210 F. 2d 139. The method, as in the Pacific Portland case, involved the charging of demurrage from the time the car was spotted for loading. The court held that the method of

operation was consistent with the tariff and established by mutual consent using this language at l. c. 395:

> "The unloaded cars were not left in the yards upon the order of defendant; such cars were not held or appropriated by defendant when they were delivered to the yard and not until they were moved from the yards and spotted for loading; and that demurrage time did begin to run actual placement at an accessible position for loading.
>
> "This was the interpretation placed on the tariffs by the plaintiff for more than 30 years. It prepared and filed its tariff. It should know what they mean, and how they should be interpreted under factual situations. There is no claim that a preference was intended by either party; and the interpretation made was in complete good faith."

In the Southern Railway case, as in the case at bar, the railway contended that its interpretation of the tariffs since 1921 had been erroneous, and the court specifically rejected the so-called "new" interpretation.

Applying the foregoing rules to this case, it is clear that Union Pacific is presumed to know the terms of its tariffs and what practices were legal and permissible thereunder. Union Pacific is the one that prepared and filed the tariffs. There is no suggestion that a preference was intended by either Union Pacific or Corneli. The interpretation was made in complete good faith, all just as in the Southern Railway case. It follows, therefore, that unless the notation of inbound references on outbound bills of lading was an absolute, fixed and exclusive method whereby the transit rate could be availed of, the carrier and shipper would be bound by their own interpretation and practice. The District Court held that the tariff created an absolute condition precedent. We shall now demonstrate that by so doing the court erred. This brings us to the second point of our argument.

II.

It is the position of Corneli that the provisions of the transit tariff were satisfied and complied with when in this case the Union Pacific required inbound references before it allowed and applied the transit rate to Corneli's transit shipments. This court has held that where there is a deviation from a tariff provision, that "adherence to form" contrary to the "plainest principles of fair dealing" and so as to produce an "unjust or absurd conclusion" is not required in arriving at the proper construction of tariffs and compliance therewith. This principle was laid down by this Court in the case of Glickfeld v. Howard Van Lines (9th Cir. 1954), 213 F. 2d 723. The Glickfeld case involved an attempt by shipper Glickfeld to recover from the Howard Van Lines full value for damaged goods when the shipping agreement contained a provision under which Glickfeld assigned a released valuation of 30¢ a pound in consideration of a reduced rate. Glickfeld undertook to escape the effect of the tariff by contending that the carrier had failed to use the specified "Uniform Household Goods Bill of Lading." The 30¢ per pound limitation had been set forth in writing in the so-called order of service, as well as the bill of lading used by Howard. The tariff filed by Howard with the Interstate Commission provided that when property was transported subject to the provision of the tariff "the acceptance and use of the uniform household goods bill of lading as described herein is required," and that "the rates shown herein are reduced rates **conditioned** upon the use of the Uniform Household Goods Bill of Lading." Instead of using the form specified in the tariff, Howard used a form of bill of lading entitled "Combined Uniform Goods Bill of Lading and Freight Bill." The form specified in the tariff contained a provision for the declaration of excess valuations of named articles for which an additional charge, not exceeding 2% of the excess value declared was required to be made,

whereas the form used by Howard provided only that all articles covered by the bill of lading were covered by the released valuation of 30¢ a pound per article. In other words, the bill of lading used contained no provision enabling a shipper to protect certain specified articles by making a declaration of excess value as to them. The evidence was that Glickfeld, the shipper, had asked for and was quoted the lowest rate, and that he had signed the so-called order of service which had printed on it in bold type the agreed or declared value was not to exceed 30¢ a pound per article. Judge Stevens, speaking for this Court, said respecting the foregoing, l. c. 727:

> "Clearly, therefore, neither the shipper nor the carrier with his insurer were prejudiced by the deviation in the form of the bill of lading used. In fact, insofar as the instant shipment was concerned, the issued bill of lading spoke the truth and covered every relevant requirement of the Interstate Commerce Act and the Commission's regulations.
>
> "While it is true that the provisions of the tariff, as published, are binding upon both the shipper and the carrier as a matter of law, those provisions are not to be read or applied in a manner which would lead to an unjust or absurd conclusion. Where the shipper has not been mislead by the deviation, or there is no allegation or proof of an intention or conspiracy to avoid the applicable law it seems to us that the denial of the reduced rate to the shipper, or the requirement that the full value should be paid for the damage would be the acme of adherence to form and contrary to the plainest principles of fair dealing . . .
>
> "The shipper was charged a rate which had been duly filed and approved by the Commission, and which was based upon a written declaration of released valuation as to the property. Since Glickfeld, the

eventual shipper, asked for and was quoted the lowest rate and, as we have already related, expressed himself as unconcerned with further details for the reason that he was himself insuring against possible shipment losses, the absence of a provision in the bill of lading for a declaration of excess value on specific items was of no primary importance. The shipper got what he bargained for, and the carrier got what it was entitled to under the statute."

Just as in the Glickfeld case, in the case at bar Union Pacific got the applicable transit rate, and Corneli paid the applicable transit rate respecting admittedly transit cargo. Neither Union Pacific nor Corneli was in any way prejudiced by Union Pacific receiving the inbound references before it applied the transit rate, even though this was after the outbound bill of lading had been issued and transit references omitted therefrom. To permit Union Pacific to collect from Corneli in this case the combined local rates on transit shipments is, in fact, a violation of the tariff and the law, and would be, as stated in the foregoing language of this court, "the acme of adherence to form and contrary to the plainest principles of fair dealing."

In Glickfeld, there was an absolute violation of the tariff in that the form required by the tariff was not used and Glickfeld therefore did not have brought to his attention the fact that he could make a declaration for an excess valuation and pay 2% additional charges. This court properly held that this deviation by the carrier did not "prejudice" the shipper, because he had agreed with the carrier as to the 30% limitation.

In the case at bar, Union Pacific could not possibly have been prejudiced by the procedure used in the allowance and application of transit rates to transit shipments.

In Loveless v. Universal Carloading & Distributing Company (10th Cir. 1955), 225 F. 2d 637, the Tenth Circuit Court of Appeals had before it a case wherein the plaintiff, Loveless, sued Universal Carloading for damages to machinery moving in interstate commerce. The standard tariff provision which the court was called upon to construe was the following:

> "As a condition precedent to recovery, claims must be filed in writing with the . . . carrier . . . within 9 months after delivery of the property . . ." and ". . . where claims are not filed . . . in accordance with the foregoing provisions, no carrier hereunder shall be liable, and such claims shall not be paid."

The shipment involved in the Loveless case was observed to have been damaged upon arrival at destination and Universal's local manager made an inspection and noted upon the consignment memo the apparent extent of the damage and signed his name. Negotiations ensued between Loveless and Universal, Loveless agreeing to accept the machinery and install it with the understanding that a formal claim for damages could be filed within 2 years. This understanding was evidenced by a letter written by the agent of the carrier, Universal. Loveless, the shipper, did not present any formal claim until 19 months after the delivery and liability was denied under the above quoted provisions of the bill of lading. The district court denied the claim. In reversing, the Tenth Circuit, speaking through Judge Murrah, pointed out that by a "practical construction" of the tariff provision it had been held to be satisfied by the courts in a variety of ways such as the exchange of telegrams and the like. He pointed out that the carrier did not contend that it had been prejudiced by failure to receive a formal claim within the 9 month period. The court held that the notation of the fact of damage on the face of the freight bill, the letter acknowledgment by the carrier that damages had been sustained, that a formal

claim would be filed at a future date, satisfied the condition precedent of the tariff respecting notice in writing. The court stated, l. c. 641, respecting its conclusion, the following:

> "Certainly it is no perversion of public policy to denominate the carrier's acknowledgment of damages and liability a claim 'in writing' to be formalized when the extent of damages is determinable. To so construe the writing leaves no doors open for abuses and discriminations which the stipulation in Sec. 2 (b) was intended to prevent. And we therefore hold the written acknowledgment of damages to be a claim in writing within the meaning and purposes of Sec. 2 (b) of the bill of lading."

The Loveless case squarely holds that so-called precedent conditions are to be practically construed, keeping in mind the purpose and objectives of the conditions. The purpose of a transit tariff is as effectually carried out by allowance and application of the transit rate after shipment as before. Indeed, all transit tariffs contain provisions for periodic audit of shippers' records after which all appropriate adjustments are made respecting transit rates. Unused transit tonnage credits are cancelled when it appears that goods inbound to transit points have been sold locally, as was the case in Utah Poultry, supra (147 F. 2d 975), or when the shipper fails to certify the product equivalent of outbound manufactured goods processed from inbound logs, as was the case in Chicago & N. W. R. Co. v. Connor Lumber & Land Co. (7th Cir. 1954), 212 F. 2d 712.

The function and purpose of the transit rate regulations is to preserve the "integrity" of the rate by procedures which protect against substitution of cargo or misuse of tonnage credits. What Union Pacific and Corneli did in this case satisfied such purposes, and the stipulated facts

expressly state that when Union Pacific allowed and applied the transit rate to Corneli's transit shipments and paid the overcharge claim this "had the result of making the effective rate of defendant's (Corneli) true transit shipments exactly what plaintiff's (Union Pacific) transit tariff authorized" (R. 17).

Inasmuch as the District Court relied on Chicago N. W. R. Co., supra, we deem it appropriate to consider the applicability of that decision. Connor Lumber Co. shipped logs to Laona, Wisconsin, a transit point, for manufacturing and reshipment. To avail itself of the transit rate it was required: (a) to ship eastbound over Chicago's line tonnage equal to inbound tonnage (except as reduced by the manufacturing process), (b) to certify the percentage in weight of outbound articles in relation to inbound tonnage, (c) to furnish the inspection bureau copies of inbound freight bills and copies of billing covering all outbound commodities. The bureau kept a debit and credit of weights inbound and outbound and cancelled the oldest inbound tonnage against outbound tonnage giving account to the product percentage, and then billed for undercharges, if any. Connor Lumber paid the transit rate on inbound logs and failed to file the certificate respecting the outbound weight percentage. It claimed the right to pay the local rate on inbound shipments selected at random and relieve itself of its obligations to continue such transit shipment outbound. It was determined by audit in 1948 that Connor Lumber had a tonnage deficit of about 30 million pounds as of December, 1947, that is, its inventory failed to equal tonnage credits by that amount, indicating a failure and inability to ship this amount of tonnage outbound over Chicago's line although bound so to do by reason of having previously shipped same inbound at the transit rate. Application of the local or non-transit rate to this tonnage gave rise to a deficit in freight rate payments of $12,152.70.

The court held Chicago Railway was entitled to collect the local rates. The District Court in the case at bar quoted with approval the following, 212 F. 2d, l. c. 717:

> "It appears that, as to all inbound shipments involved herein, defendant originally desired to and did avail itself of the transit rates plan set up by the aforesaid tariff. It thereby became obligated, in order to obtain the concession of such lower through rates to comply with every pertinent provision of the tariff imposing duties upon it as a shipper."

The context of the foregoing is revealed by the language immediately following, namely:

> "It could not accept the benefits of the program without discharging the burdens thereof. Defendant is prevented by the inherent as well as the expressed purposes of the tariff from ignoring its provision requiring the extinguishment of freight liability on in-bound shipments only in their chronological order.
>
> "Admittedly defendant's selection of certain in-bound shipments for payment of non-transit rates thereon without regard to the chronological order of such shipments would be to its financial benefit. It contends that it had the right to make that selection, urging that there is no provision in the tariff forbidding a shipper electing, at any time before claim is made by the carrier for undercharges, to pay the applicable local rates on any or all of the in-bound shipments. While there is no express language in the tariff to that effect, the principle upon which the transit rate tariff is based does not permit of such selection by a shipper of any in-bound shipments already transported under the transit tariff. Having elected to operate under that tariff as to particular in-bound shipments, he is required to comply with that tariff until all of his obligations thereunder as to such in-bound ship-

ments have been fully satisfied. Even if he makes payment of non-transit rates on selected in-bound shipments, thus attempting to free them from the tariff provisions, and the carrier actually accepts the payments under those circumstances, there is no effectual waiver. To the extent that the shipper gains a financial advantage by his attempted action, an unlawful preference results, injurious not only to the carrier but to other shippers. The carrier cannot waive the rights of other shippers. The determination as to what in-bound shipments were to be subject to the transit tariff was to be made by defendant when such shipments were made. Under item 4 (a) of the tariff the defendant could have had the shipments waybilled at non-transit rates, but it elected at the time of said shipments to avail itself of the provisions of item 4 (b) and thereby irrevocably impressed the in-bound shipments with the transit rate provisions of the tariff."

We respectfully submit that the Chicago Railway case does not support the conclusion of the District Court that the tariff in this case is "mandatory and specific as to what must be done by the shipper in order to secure the single factor or transit rate," obviously meaning thereby that inbound references could only be supplied on outbound bills of lading. In the Chicago Railway case, the transit tariff rate was availed of and applied to **normal** shipments and this gave rise to the shipper's duty to thereafter carry out its contract obligations. In the case at bar, Corneli paid the local rate inbound and outbound. When it shipped outbound it did not irrevocably "impress" the outbound shipment with the local rate. Nothing in the tariff so provided. To the contrary, the outbound shipment was a true transit shipment so known to be and so treated with respect to which the transit rate was allowed and applied when inbound references were supplied. In Chicago Rail-

road, the local rate was properly applied to local shipments not forwarded which had previously been accorded the transit rate. Just the opposite is the case at hand. The transit rate was applied to transit shipments previously paid at the local rate. Such being the facts, the Chicago Railway case does not sustain the District Court's conclusion that Corneli elected a local rate tariff or contra-wise failed to elect to avail itself of a transit tariff.

III.

The District Court assumed it was not bound by the judgment of the Interstate Commerce Commission, but nevertheless agreed with the Commission's determination that the local combination rates were not inapplicable or unreasonable. Therefore, no purpose is to be served by a separate discussion of the report of the Commission.

It is the position of Corneli that under the law this court is not bound by the judgment of either the Commission or the District Court. The facts in this case are stipulated and not in dispute. The construction and applicability of a tariff requires this Court to exercise its independent judgment. The rule is aptly stated in Sonken-Galamba Corporation v. Union Pacific R. Co. (10th Cir. 1944), 145 F. 2d 808, l. c. 812, 813:

> "The trial court found as a fact that the material shipped had value for purposes other than remelting only, and based thereon reached the legal conclusion that the shipments were not 'scrap iron' as defined in the tariff. Of course the findings of the court, if supported by substantial evidence, are conclusive here and its judgment thereon is also binding unless clearly erroneous. But the ultimate question of whether the shipments were properly classified under the tariff involves an application of the facts to the definition,

and the conclusion to be drawn therefrom, is essentially a legal concept on which this court must exercise its independent judgment."

The District Court correctly assumed that courts are not bound by the Interstate Commerce Commission's determinations. So hold Brown & Sons Lumber Company v. Louisville & N. R. Co., 299 U. S. 393, 81 L. Ed. 301, Baltimore & Ohio Railroad Co. v. Owens-Illinois Glass Company (N. D. Ohio 1954), 133 F. S. 680.

This is particularly true where the question before the Court is merely a construction of a tariff with no factual dispute and if the words to be construed in the tariff have no alleged peculiar meaning necessitating administration expertise determination. **Brown and Sons Lumber Company v. Louisville & N. R.**, 299 U. S. 393, 812 L. Ed. 301. This Court has recently affirmed this principle in the case of **Chicago, M., St. P. & P. R. Co. v. Alouette Peat Products** (9th Cir. 1958), 253 F. 2d 449.

The question presented was the applicability and lawfulness of certain tariff rates which had been determined adversely by the Interstate Commerce Commission. In holding that such a determination was not binding on this Court, it was stated, l. c. 454:

"It is to be noted that the trial court's reversal of the Commission results not from any disagreement with the Commission's findings of fact that the assailed rates were not shown to be unjust or unreasonable, but rather from the trial court's findings that the Commission's conclusion of law that the rates were not otherwise unlawful was erroneous. The conclusion of law by the Commission, which the District Court reversed, was reached by the Commission not in its quasi legislative or rate making capacity wherein it is presumed to be the expert, but in its quasi judicial capacity wherein its adjudications must be gov-

erned by applicable statutory provisions. Conclusions of law by the Commission, while entitled to respectful consideration by the Courts, do not have the same finality as its findings of fact."

CONCLUSION.

In the final analysis this case comes to this. Union Pacific's transit tariff rates were applicable to the nine carloads involved in this case and Corneli was, in fact, entitled to the transit rate. To allow and apply the transit rate Union Pacific was required to be apprised of the origin, date and weight of the inbound cargo so as to identify and charge Corneli's tonnage credits. On this record it is clear that transit rates were not allowed until after Union Pacific had the data. We submit that this was a compliance with the tariff. To hold otherwise results in applying local rates to transit shipments and this is unlawful. The latter result can only be reached in this case by a triumph of form over substance. However strictly tariffs are construed constructions are not to be such as lead to absurd and unjust results as this Court so aptly said in the Glickfeld case.

Appellant respectfully urges that the judgment of the District Court should be reversed.

Respectfully submitted,

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I certify that on the ..... day of September, 1958, I served three full, true and correct copies of the foregoing brief upon the plaintiff (appellee) by enclosing a copy in

an envelope addressed to plaintiff's (appellee's) attorney as follows:

Mr. L. H. Anderson, General Attorney,
Union Pacific Railroad Company,
Carlson Building,
P. O. Box 530,
Pocatello, Idaho,

that being his last known address, and depositing the same, postage prepaid, in the United States Post Office at St. Louis, Missouri.

.....
Counsel for Appellant.

Subscribed and sworn to before me this ..... day of September, 1958.

.....
Notary Public.

My term expires .....

No. 16108

United States Court of Appeals

FOR THE NINTH CIRCUIT

CORNELI SEED COMPANY, a corporation,
Appellant,

vs.

UNION PACIFIC RAILROAD COMPANY, a corporation,
Appellee.

Brief of Appellee

Appeal from the United States District Court
for the District of Idaho,
Southern Division.

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No. 16108

United States Court of Appeals

FOR THE NINTH CIRCUIT

CORNELI SEED COMPANY, a corporation,
Appellant,

vs.

UNION PACIFIC RAILROAD COMPANY, a corporation,
Appellee.

Brief of Appellee

JURISDICTION

The appellee agrees with appellant's jurisdictional statement.

STATEMENT OF FACTS

The appellant, Corneli Seed Company, has appealed to this court from a Judgment entered in favor of the appellee and against the appellant, dated April 14, 1958. (R. 48-49) The Judgment was entered upon an agreed statement of fact (R. 14-42).

This action was instituted by the appellee on January 19, 1955, to recover from the appellant, the sum of $3,-315.76, which the appellee had paid to the appellant upon claims presented by the appellant on nine carloads of beans, peas or shelled corn shipped from Twin Falls, Idaho, during February and March, 1953, to various points outside the State of Idaho; these shipments are detailed in Paragraph V of the agreed statement (R. 17-18) and the amounts paid to the appellant are set forth in paragraph VI (R. 18-19). Also, an additional amount sued for was $127.74, which appellant admits is due the appellee. (Paragraph VII, R. 19-20). The total amount of the suit is $3,443.50 plus interest from July 2, 1953.

After appellant's claims had been paid, the appellee concluded that appellant had not complied with the applicable tariff provision and that instead of recognizing and paying appellant's claims, it should have declined them. Accordingly, it demanded of appellant that it repay to appellee the amounts paid, which demand was refused, and upon advice that suit would be instituted to enforce collection, the appellant advised appellee that proceedings were to be instituted before the Interstate Commerce Commission to determine the applicability, reasonableness and lawfulness of the charges upon which the within action was based (Paragraph X, R. 20).

Thereafter, and on October 1, 1954, the appellant filed a complaint with the Interstate Commerce Commission challenging the application of the rates and charges upon the nine

shipments involved herein, as well as five shipments not connected with the case at Bar. Appellant alleged that the rates were "inapplicable, unjust and unreasonable," and requested the said Commission to determine "the applicable and lawful rates, and award reparation" (Paragraph XI, R. 21-22).

Then, on the 19th day of January, 1955, as heretofore stated, this action was instituted, and inasmuch as the charges set forth in appellee's complaint were being investigated by the Interstate Commerce Commission, the parties stipulated that the appellant could have twenty days from and after the decision of the Interstate Commerce Commission in which to plead to appellee's complaint, and upon this Stipulation, the trial court, on January 28, 1955, made and entered an Order in conformity with the Stipulation (Paragraph XII, R. 8-9, 22).

Upon evidence presented by the parties to the Interstate Commerce Commission, the Commission made its Report and Order on March 27, 1956, wherein the Commission found that the tariff provisions relating to transit privileges involved herein must be observed before the appellant was entitled thereto; that the appellant did not observe them, and that the "assailed rates and charges are not shown to have been or to be inapplicable, unjust or unreasonable" and, accordingly, the cause before the Commission was dismissed; a copy of the Report and Order of the Commission is attached to the agreed statement of facts, marked Exhibit "A" and made a part thereof (Paragraph XIII, R. 22-23, R. 24-42).

The appellant herein, Corneli Seed Company, petitioned the Interstate Commerce Commission for reconsideration or further hearing in that matter, and that petition was denied on August 30, 1956, and no further proceedings were taken or had by the Seed Company in that matter (Paragraph XIV, R. 23).

As already indicated, the claims of the appellant paid by the appellee, which the appellee concluded were erroneously paid and therefore resulted in this law suit involved the question of whether or not the appellant was entitled to transit privileges on the nine shipments referred to in Paragraph V, (R. 17). In other words, if the appellant Seed Company was not entitled to transit privileges, then the charges sued upon must be repaid to the appellee.

Whether the appellant was entitled to transit privileges was the question presented to the Interstate Commerce Commission, and which question has been decided by the Interstate Commerce Commission against the appellant Seed Company, because the tariff provisions relating to transit privileges were found not to be unjust or unreasonable, and that the provisions of the tariff had not been complied with by the appellant (Paragraph XIII, R. 22-23).

If transit privileges were permitted, then the appellant was entitled to the through single-factor rate from point of origin to the final destination of the shipments; that is, from the point where the commodity was originally shipped into Twin Falls, to the final destination when billed out of

Twin Falls, whereas if the transit rate was not applicable, then the appellant was required to pay the combination rate, to-wit: the rate from the original point of origin into Twin Falls, and another rate from Twin Falls to the final destination. The latter is appellee's theory, which has been sustained by the Interstate Commerce Commission, and also by the Courts as we will herein establish.

Under paragraph III of the agreed statement (R. 15), it is shown that the transit tariff provided that when shipments are made from a transit station, such as Twin Falls, the unexpired inbound freight bills which have been recorded, or the tonnage credit slips *must* be surrendered and cancelled, and in addition to that, the outbound bills of lading or shipping orders *must* have inserted thereon the weight, point of origin and date of each inbound shipment covering the commodity forwarded, and "that the transit rate would not apply if shippers fail or decline to comply with such rules and regulations."

Appellant's only asserted defense is that stated in paragraph IV of the agreed statement (R. 16-17), which is to the effect that as early as January 5, 1944, it complied with the provisions of the transit tariff referred to in paragraph III of the agreed statement (R. 15), and thereby obtained the benefit of the transit, or through rate, but discovered sometime later that by complying with the tariff, appellant's customers were enabled to ascertain and locate appellant's producers and source of supply and proceeded to make purchases direct; that in order to effect a discontinuance of this

practice, the appellant sometime in January or February, 1949, adopted a practice of making shipments out of Twin Falls, Idaho, by using the regular form of bill of lading rather than one applicable to transit shipments, which did not show the information required by the tariff and as is mentioned in paragraph III of the agreed statement of facts, which was a prerequisite to obtaining transit privileges, following which the appellant filed with the appellee its overcharge claims, and endeavored to provide some information in support of its claims, which should have been shown on the outbound bills of lading; that some of these claims were paid by the appellee until about December 15, 1953, when appellee concluded that appellant had not complied with the applicable tariff provisions, and that the claims should not have been paid (Paragraph X, R. 21). In other words, whatever practice had been followed had to be terminated because appellant had not complied with the tariff in making the shipments, and the practice appellant adopted was not provided for in the tariff.

The appellant knew about the tariff provisions, but thereafter for the reasons stated, purposely evaded them. In any event, the tariff having the effect of law, appellant was bound by its provisions, which appellee could not waive.

QUESTIONS PRESENTED

The questions presented on this appeal, in our opinion, are these:

(1) Is the Report and Order of the Interstate Commerce Commission binding on the appellant and the court, or if not

(2) Can the appellee carrier waive the plain terms or provisions of the applicable tariff, or condone a practice not authorized by the tariff?

We think our argument will demonstrate very clearly that the answer to the first question is "yes," and the answer to the second question is "no."

ARGUMENT

I

The Report and Order of the Interstate Commerce Commission is conclusive.

As a detail of the facts show, the appellant, upon advice that suit would be instituted to recover these charges, advised appellee that proceedings were to be instituted before the Interstate Commerce Commission to determine the applicability, reasonableness and lawfulness of the charges upon which the action was based, and in the complaint filed with the Interstate Commerce Commission by appellant, it was alleged that the rates were "inapplicable, unjust and unreasonable," and requested the said Commission to determine "the applicable and lawful rates, and award reparation" (Paragraph XI, R. 21-22).

The Seed Company had only one purpose in mind in proceeding before the Interstate Commerce Commission as it did,

and that was to obtain, if it could, a ruling from the Commission favorable to its contention that it was entitled to reparation and, accordingly, to use that ruling as a defense in this action. It was not successful in its attempt, for the Commission found that the "assailed rates and charges are not shown to have been or to be inapplicable, unjust or unreasonable", hence, there could be no award of reparation, and the case before the Commission was dismissed.

The proceedings before the Interstate Commerce Commission were proper. Such proceeding is authorized by law, *49 U. S. C. A. 9.* That section provides that such complaint might be brought by a person claiming to have been damaged by a common carrier either before the Commission, or before any District Court of the United States of competent jurisdiction, "but such person or persons shall not have the right to pursue both of said remedies, and must in each case elect which one of the two methods of procedure herein provided for he or they will adopt." The statute refers to any damages a person might sustain, but in the case at Bar, it was the only procedure by which the appellant Seed Company could obtain a decision with reference to whether the rates were inapplicable, unjust and unreasonable, and whether or not it was entitled to an award of reparation. If such a defense had been set up in the District Court, it would have been required to stay proceedings until the Interstate Commerce Commission had determined the matter. In this case the parties stipulated for a stay of the court proceedings to enable the Commission to determine the question presented to it by appellant.

After the Commission had finally ruled, the appellant made no effort to have the ruling reviewed by a court as it might have done under Title *28 U. S. C. A. Section 1336.* It has therefore accepted the decision of the Commission as to the five other overcharge claims (R. 29). Its effort now to have the District Court and this Court consider the matter is not a review of the proceedings of the Interstate Commerce Commission, but is a collateral attack upon the Findings and Order of the Commission, which cannot be done. If this might be termed a review, which it isn't, the evidence has not been brought to the court, and in the absence of that, we think it must be presumed the Order of the Interstate Commerce Commission is supported by substantial evidence.

Under Section *49 U. S. C. A. 9,* a shipper cannot file a proceeding in the District Court where his claim for damages necessarily involve a question of reasonableness calling for exercise of the Commission's primary jurisdiction. *United States vs. Interstate Commerce Commission,* 337 U. S. 426, 93 L. Ed 1451.

The construction and application of a tariff, the reasonableness of rates and a request for reparation award are in the exclusive primary jurisdiction of the Interstate Commerce Commission.

> *United States vs. Western P. R. Co.,* 352 U. S. 59, 1 L. Ed. (2d) 126;

> *Northwest Auto Parts Co. vs. Chicago, B. & W. R.*

Co., (8 Cir.) 240 Fed. (2d) 743; Cert. denied Oct. 14, 1957, 2 L. Ed. (2d) 32;

United States vs. Chesapeake & Ohio R. Co. (4 Cir.) 242 Fed. (2d) 732;

Armour & Co. vs. Alton RR. Co. 312 U. S. 195 85 L. Ed. 771;

Terminal Warehouse Co. vs. Pennsylvania RR. Co. 297 U. S. 500, 80 L. Ed. 827;

Johnston Seed Co. vs. United States (10 Cir.) 191 Fed. (2d) 228;

United States vs. Kansas City Southern Railway Co. (8 Cir.) 217 Fed. (2d) 763;

Callanan Road Improvement Co. vs. United States, 345 U. S. 507, 97 L. Ed. 1206;

Elbow Lake Coop. Grain Co. vs. Commodity Credit Corp. 144 Fed. Supp. 54.

The Supreme Court in *United States vs. Western P. R. Co.* supra, settled this question. The court stated, "The courts must not only refrain from making tariffs, but under certain circumstances, must decline to construe them as well," and it held, "that both the issues of tariff construction and the reasonableness of the tariff as applied, were initially matters for the Commission's determination." The ruling of the court

is, of course, based upon the fact that such matters are particularly "within the special competence of an administrative body."

> See *Interstate Commerce Com'n. vs. Martin Brothers Box Co.* (9 Cir.) 219 F. (2d) 811, 813;
>
> *Shippers' Car Supply Com. vs. Interstate Commerce Com'n.* (D. C. Or.) 160 F. Sup. 939, 943

In *Terminal Warehouse Co. vs. Pennsylvania RR Co.* supra, the court noted that the warehouse company had asked for reparation as well as for a restraining order at the hands of the Commission, and it said:

> "The Commission found, however, that no damages had been proved, and its ruling as to that was final, not subject to review by this court or any other."

The court further stated that under *49 U. S. C. A. 9,* the warehouse company had a choice between the remedy at the hands of the Commission and a remedy by suit, but that according to the statute, it could not have both. It said, "Reparation under the Commerce Act was thus permanently barred by the ruling of the Commission as against the offending carrier."

In *Johnston Seed Co. vs. United States,* supra, the finding of the Commission was that the rates charged, "were not

shown to be unreasonable," and the court stated that this "amounted to an affirmative finding that such rates were reasonable." Following which, the court said (p. 231):

> "Expediency or wisdom of the order are not elements for consideration. The field for exertion of the judicial function is exhausted when it appears that there was rational basis for the intelligent finding or conclusion of the Commission."

In *United States vs. Kansas City Southern Railway Co.* supra, the court discusses *49 U. S. C. A. 9* and states that it is recognized the Commission has jurisdiction or power to resolve an administrative question relating to any possible violations by the carrier of the Act, wholly apart from its authority to grant reparation. In other words, in the case at Bar, the Seed Company was in effect contending also that the carrier was violating the terms of the tariff, by not according it transit privileges. The Commission overruled the Seed Company's contention in that respect, for it held that the appellant had not complied with the provisions of the transit tariff and, accordingly, could not be accorded the through rate (R. 34, 36, 38). Getting back to the last case just mentioned, the court said:

> "'If he asks administratively for an award of reparations, he has, of course, made an election of recovery remedies, which leaves him thereafter without the 'right to pursue' the remedy of judicial action as such" (p. 771).

In *Callanan Road Improvement Co. vs. United States,* supra, the court said:

> "Furthermore, the appellant, having invoked the power of the Commission to approve the transfer of the amended certificate to it, is now estopped to deny the Commission's power to issue the certificate in its present form and as it existed prior to the time the appellant sought its transfer."

Also, in *United States vs. Interstate Commerce Commission,* supra, the court said:

> "It may therefore be assumed that after a shipper has elected to initiate a Commission proceeding for damages, he could not later initiate an original district court action for the same damages."

And in *Elbow Lake Coop. Grain Co. vs. Commodity Credit Corp.,* supra, the court said:

> "Where ,as here, the action of an agency is of a quasi judicial character, it is well established that the validity of its order cannot be attacked by collateral proceedings."

In this case, the appellant is asking the court to consider the same asserted defense that was presented to the Commission. Therefore, it is asking in effect, for a trial de novo. This it may not do. Its only recourse would be

to seek a judicial review of the Commission's action, which it did not do. See *Reliance Steel Products Co. vs. United States,* 150 Fed. Supp. 118, 122.

In a case where the situation was reversed, a reviewing court sustained an award of the Commission, and held that it was beyond the court's province to consider the weight of the evidence or the circumstances of the reasoning by which the Commission reached its conclusions. The court said:

> "Nor can this Court say as to the Commission's conclusion 'that its finding is unsupported by evidence or without rational basis, or rests on an erroneous construction of the statute'."

New Process Gear Corp. vs. New York Central R. Co., (2 Cir.) 250 Fed. (2d) 569, 572.

Appellant discusses this proposition under Point III in its brief commencing on Page 23. However, the cases cited are, in our opinion, not in point. The case of *Sonken-Galamba Corporation vs. Union Pacific R. Co.* (10 Cir. 1944), 145 F. (2d) 808, is not a case where the shipper was making any contention about the reasonableness of the rates and was not seeking reparation. The question in the case was which one of two rates contained in the tariff applied. The jurisdiction of the Commission under the exclusive primary jurisdiction rule was not involved. The court did construe many Commission decisions in order to

determine the proper classification of the commodity in order to arrive at the applicable rate. The court did, however, state, "Of course, we do not establish the tariff rate, nor do we judge its reasonableness, rather it is our limited province to apply the prescribed reasonable rate to the factual situation before us, and in so doing we are often required to legally interpret the definitions given us by the rate making and regulating authority."

The case of *Brown and Sons Lumber Company vs. Louisville & N. R.*, 299 U. S. 393, 81 L. Ed. 301, was one where "The simple question for decision, as to each shipment, is whether there existed 'published through rates' 'in effect from point of origin to destination.' The determination of that question requires, ordinarily merely the examination of the tariff."

That case was not one where the Commission had exclusive primary jurisdiction, for as the court said, "Here, the shippers might have brought their action at law without resort to the Commission," but the court stated that the court of appeals is bound by the decision of the Commission on questions of fact, "or questions involving exercise of administrative discretion."

In the case at Bar, the Commission not only had to rule upon the application of the tariff and its reasonableness, but also had to determine whether the practice adopted by the Seed Company was one which might result in discrimination, and it did determine that the practice could

so result (R. 38). This was the Commission's duty, not the court's.

The case of *Baltimore & Ohio R. Co. vs. Owens-Illinois Glass Co.*, 133 Fed. Supp. 680, really confirms appellee's position. The facts distinguish the case from the one at bar, but the court did not deviate from the holdings in the decisions we have cited in connection with the exclusive primary jurisdiction rule. The court referred to the decision of the Supreme Court in *Texas & Pacific Ry. Co. vs. Abilene Cotton Oil Co.*, 204 U. S. 426, 51 L. Ed. 553, which held that a shipper could not maintain an action at common law for excessive and unreasonable freight rates on interstate shipments "where the rates charged are those which had been duly fixed by the carrier according to the Act and had not been found to be unreasonable by the Interstate Commerce Commission" (p. 690).

The case of *Chicago, M., St. P. & P. R. Co. vs. Alouette Peat Products* (9 Cir. 1958), 253 F. (2d) 449, is clearly distinguishable. First of all, that case arose out of a direct attack, (not collateral), upon the Order of the Commission, and while the Commission first found that the rates were unjust and unreasonable and ordered reparation and then reversed itself and found that it had not been shown that the rates were unjust or unreasonable, nevertheless, the Commission found, that the rates in question were placed in a tariff which was not a legal tariff, because the tariff attempted to make the rates effective upon five day's notice instead of thirty day's notice as the statute required. The Commission

could not violate the mandatory requirement of the law. In the last paragraph of the court's opinion it is said, "The short answer to this specification of error is that it was not the trial court who found that the railroad failed to comply with the Order in Ex Parte 162, but it was the Commission, and the Commission's finding in that respect is final and conclusive."

The court also held that shippers had always been required to pay the rates specified in the tariff and quotes in a foot note from the case of *Davis vs. Portland Seed Company,* 264 U. S. 403, 425, 68 L. Ed. 762 as follows. "The statute required rigid observance of the tariff, without regard to the inherent lawfulness of the rates specified." In the case at Bar, the provisions of the tariff were not followed and as we will show, and as appellant has already admitted on page 9 of its brief, the "carrier cannot be estopped or waive collection of applicable rates." Neither can it waive rules and regulations set forth in the tariff.

The difference between the cases cited by appellant and those which we have cited herein are that different principles are involved as illustrated by the statement contained in the case of *Great Northern Ry Co. vs. Merchants' Elevator Co.,* 259 U. S. 285, 291, 42 S. Ct. 477, 66 L. Ed. 943, referred to in the case of *Baltimore & Ohio R. Co. vs. Owens-Illinois Glass Co.,* supra, wherein the Supreme Court stated, "Whenever a *rate, rule,* or *practice* is attacked as unreasonable or as unjustly discriminatory, there must be preliminary resort to the Commission." (Emphasis supplied) In the case at Bar,

the appellant, before the Commission, attacked the rate and the rule under the tariff and, in effect, asked the Commission to sanction the practice which it was following in not complying with the rules of the tariff. The Commission not only held that the rates were not unreasonable and also that the claim procedure practice adopted by the appellant offered "opportunities for irregularities which are minimized by the established transit rules" (R. 38).

2.

The Appellee Carrier Could Not Waive the Provisions of the Applicable Tariff, or condone a practice not authorized by the tariff.

The carrier not only cannot waive the provisions of a tariff, neither can it allow a practice or privilege to exist which is not set forth in the tariff.

This action is based upon the provisions of *49 U. S. C. A. 6 (7)* which provides that no carrier can participate in transportation of passengers or property, unless its rates are published in a tariff; it must charge and collect no more and no less than the tariff provides,

> "nor shall any carrier refund or remit in any manner or by any device any portion of the rates, fares, and charges so specified, nor extend to any shipper or person any privileges or facilities in the transportation of passengers or property, except such as are specified in such tariffs" 49 USCA 6 (7).

Appellant's defense in this action is based entirely upon what is stated in paragraph IV of the agreed statement of facts (R. 16), and the argument that it now makes is that the appellee is estopped to deny the practice which the appellant's representative adopted as mentioned in the agreed statement of facts, or that the appellee carrier waived the plain provisions of the transit tariff. That this cannot be done is admitted by appellant in its brief at the bottom of page 9. In other words, appellant is now contending that because of the conduct of the parties with reference to the practice which appellant's representative adopted, appellee cannot now be heard to say that such a practice was wrong.

The decision of the Interstate Commerce Commission, irrespective of whether the exclusive primary jurisdiction rule prevails, was correct as a matter of law. Judge Taylor's opinion (R. 42-48) *161 Fed. Supp. 52,* is not only a well written opinion, but is also correct, for under the authorities and, in fact, the admission made by appellant, the decision of the Commission and the court, could not have been otherwise.

The agreed statement of facts sets forth the rules and regulations of the transit tariff which is "that when shipments *are forwarded* from the transit station, unexpired inbound freight bills, which have been recorded, or tonnage credit slips *must* be surrendered and canceled; that the outbound bill of lading or shipping order *must* have inserted thereon the weight, point of origin, and date of each inbound shipment covering the commodities forwarded *and that the transit rate will not apply if shippers fail or decline to comply*

with all rules and regulations." (Emphasis supplied). (R 27, 28).

This tariff says plainly what must be done, "when shipments are forwarded from the transit station," not that the information is to be supplied sometime later with claims that are filed. It is admitted that the provisions of the tariff were not complied with at the time the shipments were forwarded from Twin Falls, and the tariff definitely states that the transit rate would not apply if the shippers fail or decline to comply with all the rules and regulations.

Consistent with the law, the Interstate Commerce Commission held, "Departures from the rules and regulations of the published tariff were not justified, even though the claim procedure may have been approved by an agent of the defendants. The tariff's provisions must be observed" (R. 34). The word "defendants" referred to by the Commission, of course, were the carriers. This statement by the Commission further emphasized that the defense of appellant has reference to the conduct of the parties. This court stated in *National Carloading Corp. vs. Atchison T. & S. F. Ry. Co.*, 150 Fed. (2d) 210:

> "It should be noted here that conduct, intention, mistake and misunderstanding are no defense to such an action."

In that case, the Interstate Commerce Commission broke up what it said was an illegal practice by the carrier, just as

the appellee in this case stopped an illegal practice which existed, and then sued to recover the proper charges.

Similarly, this court in *West Coast Products Corp. vs. Southern Pacific Co.*, 226 Fed. (2d) 830, said:

> "There is a suggestion in the record that in the past such shipments have been carried under the tariff description now claimed to be applicable by West Coast. Whether or not this is reasonably explained makes no difference. The carrier is not subject to estoppel. The law requires the railroad to charge and collect the applicable rate irrespective of erroneous interpretations in the past. Otherwise, the policy against the allowance of rebate might be violated."

We think these two cases are conclusive. This court, also, in the case of *Northern Pacific Ry. Co., vs. Mackie,* 195 F. (2d) 641, held that the provisions of the bill of lading relating to claims must be complied with, and "that the carrier cannot waive the provision." The court also said in that case:

> "A vital purpose of the Interstate Commerce Act is to prevent preferences and discriminations by carriers as among shippers. For the carrier to disregard the condition precedent to recovery incorporated in the bill of lading here would, under the circumstances shown, open the door to evasion of the spirit and purpose of the Act in the respects mentioned."

That statement, of course is consistent with the cases cited by Judge Taylor in his memorandum opinion (R. 45-46). We think the case of *Lowden vs. Simonds-Shields-Lonsdale Grain Co.*, 306 U. S. 516, 83 L. Ed. 953, 957, is particularly applicable. The Supreme Court in that case stated that, "It is equally important to aid the efforts of a carrier in collecting published charges in full."

See also, *Louisville & N. R. Co. vs. Maxwell,* 237 U. S. 94, 59 L. Ed 853.

The rules and regulations of a tariff are just as important as the rate named. The rules and regulations in a great many cases, and that is true in this case, affect the rate and determine which rate is applicable.

Probably the most recent statement by the Supreme Court is contained in *United States vs. Western P. R. Company,* 352 U. S. 59, 1 L. Ed. (2d) 126, and in Note 20 on page 139 of the Law Edition Report, to the effect that under the Interstate Commerce Commission Act, *49 U. S. C. A. 6 (7),* a shipper may not invoke the defense of estoppel and that the Act forbids "departures from the published tariff."

Appellant is endeavoring to sustain its defense on equity principles. Under the provisions of the Interstate Commerce Commission's Act "the legality of the rate claimed applicable is not dependent upon the equities involved." *Armour & Co. vs. Atkinson, Topeka & Santa Fe Ry. Co.* (7 Cir.) 254 F. (2d) 719, 723.

In addition to the question of waiver or estoppel, there is another question equally important, and that has reference to the so-called claim procedure which the appellant followed and which was adopted by its representative to avoid the plain provisions of the tariff. This claim procedure appellant adopted was a privilege which, for a time at least, the appellee carrier extended to appellant, but without such privilege or arrangement having been authorized by or set forth in the tariff.

The Commission found that this claim procedure and settlement was, "not authorized by the applicable transit tariff" (R. 28).

The last part of *49 U. S. C. A. 6 (7)* states that a carrier may not refund or remit in any manner or by any device any portion of the rates "nor extend to any shipper or person any privileges or facilities in the transportation of passengers or property except such as are specified in such tariffs." The privilege or practice adopted by the appellant was not specified in any tariff and, accordingly, was illegal. One of the purposes of the enactment of the Interstate Commerce Commission Act was to prevent any secret or side arrangements between a shipper and a carrier, and that is the reason that all rules, regulations, privileges and rates must be set out in the tariff so that there can be no discrimination. Under the practice adopted by appellant in this case, there being nothing in the tariff concerning it, the carrier could have permitted the practice to exist as it did for awhile with appellant, and in another case refuse to permit it. As the Supreme

Court said in *Armour & Co. vs. Alton R. Co.*, 312 U. S. 195, 85 L. Ed. 771, 775:

> "The complaint shows that there is no provision in the tariff which would authorize the railroads to make refunds to petitioner of those charges paid by petitioner to the Stock Yards Company. Such refunds, if made, would be in the nature of special allowances not authorized by the tariff. A court's adjudication of this question in this case would not uniformly benefit all shippers for whom respondents have transported livestock. Whether or not such a refund would amount to a discrimination should be determined by studies such as those the Interstate Commerce Commission is especially empowered to make."

As mentioned by the Interstate Commerce Commission (R. 38), transit arrangements have been a source of discrimination and that uniform rules and regulations in tariffs are necessary to afford equal opportunities to all shippers. The Commission also stated that the rules and regulations have played an essential part "in the maintenance of equality of charges for competing transit operators," and then concludes:

> "Obviously, the desired claim procedure offers opportunities for irregularities which are minimized by the established transit rules. It would impose greater administrative obligations on the defendants in policing transit arrangements and making repayments

based on the through single-factor rates, and has no sound evidentiary support" (R. 38, 39).

In *Oregon-Washington R. & Nav. Co., vs. C. M. Kopp Co.* (Wash.) 120 Pac. (2d) 845, 138 A. L. R. 633, the court held that a carrier's promise to notify a purchaser when his order of diversion is accomplished was discriminatory and void because such a service was not contained in the published tariff. It was so held notwithstanding the carrier's custom to enter into agreement to notify shippers of the accomplishment of such orders. In that case the court refers to *49 U. S. C. A. 6 (7)*, and also cites the case of *Chicago & Alton R. R., vs. Kirby,* 225 U. S. 155, 56 L. Ed. 1033 in which it is said:

> "A shipper is presumed to know what the published rates are, and if they do not contain provisions for the special service guaranteed to him he must be taken as having contracted for a rate discriminatory in his favor."

In the Kopp case it was asserted that respondent's custom to enter into agreement with shippers to notify them of the accomplishment of diversion orders did not result in any preference to Kopp or discrimination in his favor, just the same as the defendant argues in this case. However, the Supreme Court of Washington said that such an argument was foreclosed by the opinion of the Supreme Court in *Davis vs. Cornwell,* 264 U. S. 560, 68 L. Ed. 848, in which the court quotes from the Kirby case, stating that a special contract to

transport a car by a particular train on a particular day is illegal when not provided for in the tariff;

> "The contract to supply cars for loading on a day named provides for a special advantage to the particular shipper, as much as a contract to expedite the cars when loaded. *It was not necessary to prove that a preference resulted in fact. The assumption by the carrier of the additional obligation was necessarily a preference.* * * * The paramount requirement that tariff provisions be strictly adhered to, so that shippers may receive equal treatment, presents an insuperable obstacle to recovery" (Emphasis supplied).

In *Davis vs. Henderson,* 266 U. S. 92, 69 L. Ed. 182, Henderson sued the Railroad for damages because it failed to furnish a car within a reasonable time after notice. The carrier defended on the ground that the shipper had not complied with the rule contained in its tariff, which provided that orders for cars must be placed in writing. Written notice was not given. The Supreme Court reversed a judgment in favor of Henderson, saying:

> "The contention is that the rule was waived. It could not be. The transportation service to be performed was that of common carrier under published tariffs. The rule was a part of the tariff."

Also in point, we think, is the case of *Pennsylvania R.*

Co. vs. International Coal Mining Co., 230 U. S. 184, 57 L. Ed. 1446.

The law is clear. The Commission and Judge Taylor were correct.

(Appellant's Point I, Pages 9-14)

In our opinion, appellant has cited no cases which support its theory. It refers to the case of *Utah Poultry Producers Corp. vs. Union Pacific R. Co.* (10 Cir. 1945), 147 F. (2d) 975, and quotes part of the decision. This decision, in our opinion, is authority for appellee. According to that opinion, it is for each railroad to determine whether transit privileges will be allowed "and the conditions under which it may be exercised," which means that the rules and regulations governing the privileges must be set out clearly in the tariff. It does not mean that the carrier can set out the conditions in the tariff and then ignore them, or that the shipper can obtain the benefit of the privilege without complying with the conditions, or by substituting a procedure contrary to the provisions of the tariff. In the Poultry Producer's case, the court said:

> "It follows that the tariff granting transit priviliges determine the nature of the rights conferred thereby, and that when the character and extent of these rights come into question we must seek the answer within the four corners of the published tariff itself."

A little later the court also said:

> "Transit privileges grant special concessions to the shipper. In permitting them, the Interstate Commerce Commission has been zealous in protecting the integrity of the through rate. It is made plain in all its decisions that unless such privileges are carefully circumscribed, they permit opening the doors to discrimination and thus tend to destroy the integrity of the through rate."

Appellant also cites the case of *Pacific Portland Cement Company vs. Western Pacific Railroad Company* (9 Cir. 1950), 184 F. (2d) 35, which involves a situation regarding demurrage charges. This case is clearly distinguishable from the facts in the case at Bar. In that case, a railroad company ordinarily held cars for prospective loading by the cement company on the railroad's own track at Gerlach, Nevada, and supplied cars to the cement company on its own private tracks whenever the cement company placed orders for the cars with the railroad. Congestion developed in the railroad yards at Gerlach, so the railroad, solely for its own benefit, asked permission of the cement company to store cars on the cement company's track to relieve the railroad congestion. Later, a railroad representative concluded that demurrage on the cars loaded by the cement company should be determined from the time the railroad placed the cars for storage on the cement company's track, rather than from the time orders were placed for cars and they were appropriated by the cement company. If the cars had remained on the rail-

road's track in storage, demurrage would have been determined from the time the car order was placed and the car appropriated for loading by the cement company. The court refused to permit the carrier to recover the demurrage charges on the basis mentioned, and it was right in so doing, for under the tariff, "the time on which demurrage charges are based did not commence to run until appellant spotted the cars for loading."

The court did not stray in the least from the principles of law governing tariffs and matters under the Interstate Commerce Commission's Act, for it said:

> "We agree that published tariffs are binding on both carrier and shipper *and that the shipper's liability under such tariffs cannot be waived by any arrangement, understanding or course of conduct between the parties.* (Citing 49 U. S. C. A. 6 (7) and other cases.) (Emphasis supplied).

To make the decision of the court clearer, it further stated:

> "It is no less true, however, that the tariffs themselves impose no liability for demurrage under the facts of the instant case."

The court said that a contrary holding would result in the shipper being held liable to the railroad for a service which the shipper had rendered to the railroad, but as a matter of

fact, there was no violation of the tariff.

The statement quoted by appellant on page 13 of its brief, we think, was wholly unnecessary to a decision of the case, because having previously held that the tariff imposed no liability for demurrage, that ended the matter.

The case of *Southern Ry. Co., vs. Aluminum Co. of America,* 119 F. Supp. 389, affirmed (6 Cir.) 210 Fed (2d) 139, cited by appellant is similar to the *Pacific Portland Cement Company* case. The tariff had not been violated and, hence, no demurrage was due the carrier.

Contrary to appellant's contention, the carrier, as we have shown, could not legally interpret the tariff contrary to its plain provisions and purposes, and neither could it waive such provisions, or, by its conduct, condone a practice (the claim procedure) which was not set forth in the tariff.

(Appellant's Point II, pages 15-23.)

In the case of *Glickfield vs. Howard Van Lines* (9 Cir. 1954), 213 F. (2d) 723, the tariff stated that the reduced rates were "conditioned upon the use of the uniform household goods bill of lading," nevertheless, the carrier issued its "*combined* uniform household goods bill of lading *and freight bill*" which, as the court mentioned, was "subject to the classification and tariffs, rules and regulations in effect on the date of the issue of this bill of lading." This bill of lading, therefore, contained what the tariff mentioned and a little more—not less. We have emphasized the parts added

apparently by the carrier which did not detract from the requirements of the tariff. What really distinguishes the Glickfield case from the one at Bar is this statement by the court, "In fact, insofar as the instant shipment was concerned, the issued bill of lading spoke the truth and covered every relevant requirement of the Interstate Commerce Act and the Commission's regulations." That statement cannot be made in the case at Bar. None of the tariff requirements were complied with, and there was no tariff authority for the claim procedure which was adopted. In the Glickfield case there could be no chance for a conspiracy or intention to avoid the applicable law, for it was complied with. All shippers were openly treated the same.

In the case at Bar, unless the evidence was supplied at the time the bill of lading was issued and when the shipments were tendered to the carrier at Twin Falls, there was no way in which the carrier could determine whether the shipments were entitled to the transit rate. After the shipments had moved from Twin Falls, this could not be determined.

In the Glickfield case, the court further said, "The shipper was charged a rate which had been duly filed and approved by the Commission, and was based upon a written declaration of released valuation as to the property," which established what the court had previously said, that "every relevant requirement of the Interstate Commerce Act and the Commission's regulations had been fully complied with." That case involved neither rates, reparations, rebates or discriminations. Appellant, by its own plan to evade the tariff,

and without complying with the tariff, obtained an advantage no other shipper had or might obtain, for appellant's plan was not contained in the tariff as the Act, *49 U. S. C. A. 6 (7)* requires.

The case of *Loveless vs. Universal Carloading & Distributing Company* (10 Cir. 1955), 225 F. (2d) 637, cited by appellant has no application to the case at Bar. The court does refer to *Northern Pac. Ry. Co. vs. Mackie,* (9 Cir.) 195 Fed. (2d) 641, to which we have previously referred, and which holds that the bill of lading provisions with reference to presentation of claims must be complied with by the claimant, and "that the carrier cannot waive the provisions." In the Loveless case there was clear liability and an express admission thereof, together with a written memorandum from the carrier's agent which in part stated that the memorandum "will protect you in the event claim will be filed, for a period of up to two years." The carrier's agent stated that he had notified the carriers that a claim would be filed. The court held that to satisfy the provision of the bill of lading the writing need not be in any particular form and that what was done was sufficient to apprise the carrier that damages had occured for which an award of damages could be expected; that the purpose of the filing of the claims under the provisions of the bill of lading was to enable the carrier to make an investigation, and that that had been accomplished. The Loveless case clearly has no application to the case at Bar. There was no intentional or other disobedience of the tariff, neither was there a plan of procedure to obtain

privileges which were not published in a tariff, such as in the case at Bar.

The Loveless case is based almost entirely upon the Hopper case, and the Hopper case has been questioned many times, whereas the Mackie decision of this court has not. *East Texas Motor Freight Lines vs. United States* (5 Cir.) 239 F. (2d) 417, 420.

Appellant makes an effort to distinguish the case of *Chicago & N. W. R. Co. vs. Connor Lumber & Land Co.* (7 Cir.) 212 Fed. (2d) 712, but we think that cannot be done, for the law as announced in that decision is, "* * * a transit privilege is not a matter of right; and all conditions and limitations prescribed with reference to it must be observed", and as further quoted by Judge Taylor in his opinion where the situation was quite similar to the case at Bar because the defendant in that case had originally desired to, and did, avail itself of the transit rate's plan set up in the tariff, "it thereby became obligated in order to obtain the concession of such lower through rates to comply with every pertinent provisions of the tariff imposing duties upon it as a shipper."

Another case which has not been referred to and which cannot be distinguished from the case at Bar is *Tex-O-Kan Flour Mills Co., vs. Texas & P. Ry. Co.* (5 Cir.) 178 Fed. (2d) 89.

CONCLUSION

We think that a comparison of what the tariff requires

(R. 15, 27-28) with the information appellant says was supplied with each claim (R. 16) establishes that there was not even a compliance with the tariff when the claims were filed after the shipments were made, but in any event, the Interstate Commerce Commission had exclusive jurisdiction of the issues it was called upon to decide and its Findings and Order are conclusive. Judge Taylor found it unnecessary to decide that issue because he agreed that the holding of the Commission was correct. We think the Commission and the trial judge could have decided no other way and stayed within the law. That the judgment of the trial court must be affirmed is

Respectfully submitted,

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No. 16,108.

IN THE

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT.

CORNELI SEED COMPANY,
Appellant,

vs.

UNION PACIFIC RAILROAD COMPANY,
Appellee.

Appeal from the United States District Court for the District of Idaho, Southern Division.

REPLY BRIEF OF APPELLANT.

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REPLY BRIEF OF APPELLANT.

Appellee, Union Pacific, devotes its brief to two questions which are stated as follows:

> "1. Is the report and order of the Interstate Commerce Commission binding on the appellant and the court, or if not
>
> 2. Can the appellant carrier waive the plain terms or provisions of the applicable tariff, or condone a practice not authorized by the tariff?" (Appellee's brief, page 7).

The first question posed by Union Pacific joins issue with the appellant Corneli's Point III which asserts that this record presents only a question of law as to the interpretation of the tariff in question by reason of which neither the decision of the Interstate Commerce Commission, nor the District Court, is binding on this court.

Corneli submits the second question raises a false issue. It assumes that Corneli's contention is that Union Pacific waived or condoned a practice not authorized by the tariff.

Such is not the case. Corneli agrees that under the law Union Pacific could not waive compliance with tariff requirements (Corneli's brief, page 9). The question is not waiver, but rather whether or not the construction and practice mutually adopted by Union Pacific and Corneli whereby the transit tariff was complied with by furnishing inbound references after shipment rather than on outbound bills of lading, was a compliance with the tariff.

I.

We first consider Union Pacific's first contention that the decision of the Interstate Commerce Commission is binding on Corneli and this court. Inasmuch as the courts in some of the cases cited by Union Pacific and in the quotations printed in the brief, speak in terms of "estoppel," "res judicata," "election of remedies," "primary jurisdiction" and the "negative order doctrine," it will be helpful to first have in mind the meaning of these terms and doctrines before discussing the applicability of the decisions relied on. In 42 American Jurisprudence at page 698, paragraph 254, the doctrine of primary administrative jurisdiction is defined as follows:

> "The doctrine of primary jurisdiction is that the courts cannot or will not determine a controversy involving a question which is within the jurisdiction of an administrative tribunal prior to the decision of that question by the administrative tribunal, where the question demands the exercise of sound administrative discretion requiring the special knowledge, experience, and services of the administrative tribunal to determine technical and intricate matters of fact, and a uniformity of ruling is essential to comply with the purposes of the regulatory statute administered."

In 42 American Jurisprudence at page 593, paragraph 202, the negative order doctrine is defined as follows:

> "Until the decision in Rochester Telephone Corp. v. United States was handed down, the right to judicial

review of administrative action was narrowed to a considerable extent by the so-called 'negative order' doctrine, under which Federal courts had denied their jurisdiction to review 'negative orders,' that is, orders in which the administrative authority merely refused to grant the relief sought. . . . The negative order doctrine rested primarily on two considerations, one involving the interpretation of the terms of the controlling statute which was construed to confer upon the court no jurisdiction to review orders requiring no affirmative action for their enforcement, and the other involving the erroneous assumption that review of a negative order would amount to a judicial determination de novo of the right to relief and thus constitute an exercise by the courts of administrative authority."

In 42 American Jurisprudence, page 703, paragraph 255, the principle respecting election of remedies is stated as follows:

"Where a remedy in the judicial or in the administrative forum is available to the same party in the same situation, he has his choice as to which remedy he will take. Sometimes the statute itself provides that a party must elect between the remedies and may not avail himself of both. Under such a statute, a party who elects to proceed before the administrative tribunal and is denied relief on the merits there, may not later bring the common-law action which he might have chosen in the first instance, and one who obtains relief on his claim in the administrative tribunal is bound by such award and may not later institute a common-law action to seek additional relief on the same claim."

49 U. S. C. A., Section 9, provides a shipper claiming to be damaged by a carrier may file a complaint either with the Commission or sue in a District Court. It is this sec-

tion which gives rise to Union Pacific's contention respecting election of remedies.

Another statutory principle in the scheme of adjudication of rights between carriers and shippers is that when reparations are awarded a shipper he must then sue the carrier for damages in the District Court, and although the Commission's reparation order makes a prima facie case the trial is de novo and by jury if desired. The action is in tort for damages [49 U. S. C. A., Section 16, Par. (2)]. Formerly when the relief was denied by the Commission and a claim dismissed, there was no judicial review under the Negative Order Doctrine. To correct this obvious disparity of treatment the United States Supreme Court repudiated the Negative Order Doctrine and the shipper may now have judicial review. United States v. Interstate Commerce Commission, 337 U. S. 426, 93 L. Ed. 1451. It is also the law that the Commission has no jurisdiction to determine the liability of a shipper to a carrier, and that the courts have exclusive jurisdiction. The rule is stated as follows in Pennsylvania Railroad Company v. Fox & London, Inc., (2nd Cir. 1938), 93 F. 2d 669, l. c. 670:

> "Of course, the Interstate Commerce Commission only has such jurisdiction as has been conferred upon it by Congress, and that does not give it the power to make orders adjudicating claims of carriers against shippers and requiring the payment of such claims. See Davis v. Rochester Can Co., 220 App. Div. 487, 221 N. Y. S. 666, affirmed Mellon v. Rochester Can Co., 247 N. Y. 521, 161 N. E. 166; Laning-Harris Coal & Grain Co. v. St. Louis & San Francisco R. Co., 15 I. C. C. 37. So jurisdiction of such a controversy as this is vested exclusively in the courts."

The foregoing principle gives the shipper full opportunity to defend in court. The carrier's action is in contract.

Union Pacific's first contention may be summarized as follows:

1. That the Commission had exclusive "primary jurisdiction" of Corneli's complaint seeking to establish new routes and determine applicable and lawful rates for same and also for a determination that the combination of rates to and from Twin Falls were inapplicable, unjust and unreasonable and if so to grant reparations.

2. That the denial of reparations by dismissal of Corneli's petition was a final order not reviewed and constitutes the exercise of primary Commission jurisdiction such as to conclusively bind Corneli and effectively deprive it of any defense to Union Pacific's suit because (a) Corneli **elected** to bring the proceeding before the Commission, or (b) because Corneli is **estopped** by the Commission's order, or (c) because if Corneli denies the conclusiveness of the Commission's action this constitutes a collateral attack which cannot be made.

We shall show that the Union Pacific's position in each and all of the foregoing respects is untenable. First, as to the question of "primary jurisdiction." The complaint which Corneli made before the Commission was that the routes were unreasonably long, and that the rates and charges of Union Pacific, including those on the 14 shipments involved, were therefore unjust and unreasonable, and that a new route through Wells, Nevada, should be ordered and rates established. In addition, Corneli claimed that the combination rates were improperly applied to the shipments in question and were unjust and unreasonable and reparations should be granted (R. 26). The Commission denied the establishment of a new route and dismissed the complaint and did not grant reparations. In its report the Commission said that Union Pacific's transit tariff was not applicable because not complied with, and that the local rates paid in and out of Twin Falls were not shown to have been or to be inapplicable, unjust or unreasonable.

Under the teaching of Great Northern Railway Company v. Merchant's Elevator Company, 259 U. S. 285, 66 L. Ed.

943, l. c. 946, the dismissal by the Commission with respect to the establishment of a new route and fixing rates was obviously legislative and administrative, prospective in character, and within the exclusive jurisdiction of the Commission so as to require its action. The question as to whether the transit tariff had been complied with, that is to say, the applicability of the combined rates where the facts are undisputed, raised a question of law respecting which the courts may act notwithstanding resort to the Commission. In such circumstances the Commission's decision is open to judicial inquiry, since a question of law rather than fact is involved, the facts being undisputed. The election under Section 9 of 49 U. S. C. A. only precluded Corneli from thereafter **initiating** an action in a District Court. This distinction is clearly noted in the case of United States v. Interstate Commerce Commission, 337 U. S. 426, 93 L. Ed. 1451 at l. c. 1459, where the court says that a shipper "could not later **initiate** an original District Court action for the same damages." The statute does not say that a claim for reparations is an election which bars a shipper from **defending** a lawsuit required by law to be brought by the carrier in a District Court. No court has ever so held. Estoppel, res judicata, or election of inconsistent remedies are matters of defense. The controlling case on facts is Baltimore & Ohio Railroad Company v. Owens-Illinois Glass Company (N. D. Ohio 1954), 133 F. Supp. 680, referred to in Corneli's original brief. In the Baltimore case the railroad, as Union Pacific did in this case, sued for failure to pay the so-called lawful rates on shipments of sand. As in the case at bar defendant defended on the ground that the lawful applicable rates had been paid, and that the charges the plaintiff railroad sought to recover were in excess of the lawful charges provided by the lawfully applicable tariff. In the Baltimore case, as here, the railroad claimed the conclusiveness of a prior decision of the Interstate Commerce Commission on the theory that the matter had been decided by the Commis-

sion as a matter of primary jurisdiction. The Commission had decided in favor of the railroad and denied reparation claims and no review was sought. The scholarly opinion of Special Master Fred H. Kruse, which was adopted by the court in the Baltimore case, is an exhaustive and comprehensive analysis of the case law respecting the problem, and contains a review of the cases. The court held, 133 F. Supp., l. c. 691:

> "We cannot agree with the contention of counsel for the plaintiffs that the determination by the Interstate Commerce Commission should be considered as controlling on this court for the reason that the case there was one within the primary jurisdiction of the Commission in which it had to consider matters of fact and extrinsic evidence and applied its expert knowledge in order to determine the issue involved; that its decision involved questions of fact as to the type of sand shipped, the intent of the railroads in their petitions for increase and the intent of the Commission in granting such increase, the reason for the difference in rates when different equipment was used, and the technical meaning of the term 'Noibn' used in the master tariffs. It seems to us that these contentions cannot be sustained, because these matters were not in controversy in this case."

Respecting the application of the principle of res judicata or estoppel by judgment, the court said, l. c. 693:

> "It is apparent that the facts in the case at bar are different from the cases above discussed, and the question remains whether, on the principle of res judicata or estoppel by judgment, this court is controlled by the decision of the Interstate Commerce Commission in the Anchor Hocking Case. (Citing cases.) It would appear from the reports that the principle of res judicata or estoppel by judgment applicable to decisions of the courts has not been applied to determinations of

the Interstate Commerce Commission or administrative agencies generally."

The court concludes at l. c. 695 as follows:

> "Our conclusion is that under the present state of the law, the determination by the Interstate Commerce Commission in the Anchor Hocking case on the question of law as to the construction of the tariffs involved here is not res judicata or controlling on the court in this case."

Corneli respectfully submits that a careful reading of the 23-page opinion in the Baltimore case leads inevitably to the conclusion that the doctrine of the **Great Northern Railway Company v. Merchants' Elevator Co.**, 259 U. S. 285, 66 L. Ed. 943, is controlling, and that the construction of the Commission is not conclusive in this case because there is no dispute of fact with respect to what the parties did. The only question being whether the transit tariff was thereby complied with.

Union Pacific's reliance on Terminal Warehouse Company v. Pennsylvania Railroad Company, 297 U. S. 500, 80 L. Ed. 827, to the effect that when the Commission finds no damage in a reparation case that its ruling is final and not subject to judicial examination by a court is completely without substance because the Terminal Warehouse case was decided before the Negative Order Doctrine was repudiated, and the Terminal case is simply one of the many cases that were overruled when the court abandoned the idea that denial of reparations relief by the Commission was administratively final and not subject to judicial inquiry. This matter is fully discussed in United States v. Interstate Commerce Commission, 93 L. Ed., l. c. 1462, footnote 8.

Mr. Justice Harlin in the United States v. Western Pacific Railroad Company, 352 U. S. 59, 1 L. Ed. 2d 126, states that "in cases raising issues of fact not within the

conventional experience of judges or requiring the exercise of administrative discretion, agencies created by Congress for regulating the subject matter should not be passed over . . .''; that primary jurisdiction is ''a doctrine allocating law making power'' (1 L. Ed. 2d, l. c. 132). The field respecting the power of courts to pass on tariff construction as issues of law is recognized and said to have ''emerged'' in Great Northern R. Co. v. Merchants Elevator Co., 259 U. S. 285, 66 L. Ed. 943. Corneli submits that there is no special administrative competence involved in deciding whether or not what the parties did in this case was a compliance with the transit tariff as a matter of law.

We consider first the cases cited by Union Pacific involving the allocation of jurisdiction. In United States v. Western P. R. Co., 352 U. S. 59, 1 L. Ed. 2d 126, the question was whether certain bomb cases should be classified under a tariff rate for incendiaries or whether they should be classified under a lower tariff rate. In discussing the doctrine of primary jurisdiction the court noted that one of the contentions of the shipper was that the higher rate, if applied, would be ''unreasonable'', thereby intertwining the questions of classification and reasonableness. Because of the complexity of cost factors underlying such a determination, the court correctly concluded that the question should be presented to the Commission in the first instance. The appellant is in complete accord with the principles enunciated in this case. As applied to the case at bar, the question of reasonableness has been presented to the Commission. The only question now before this Court is the construction of the tariff provision on undisputed facts which may be done as a simple matter of law.

In Northwest Auto Parts Co. v. Chicago B. & W. R. Co., 240 F. 2d 743 (8th Cir.), the court in line with Western Pacific decided that the question of classification of scrap under a particular tariff, which also presented a question

of reasonableness, should be referred initially to the Commission.

In United States v. Chesapeake & Ohio Railway Co. (4th Cir. 1957), 242 F. 2d 732, the record failed to show whether or not expert knowledge was required and the court merely remanded the case to the District Court with directions to retain jurisdiction while the question of reasonableness was presented initially to the Commission. This was done merely because in the case at bar the Commission determined questions of reasonableness.

In United States v. Kansas City Southern Railway Co. (8th Cir. 1955), 217 F. 2d 763, a shipper sought to recover for terminal services not actually furnished at the port of shipment. The granting of such an allowance would have clearly involved Commission competence respecting questions of cost allocation since the recovery would have permitted the shipper to obtain a rate lower than the only tariff rate available. The court properly held that the case should be remanded to the District Court with a retention of jurisdiction while the administrative question was referred to the Commission. This case sustains Corneli's contention in that it shows certain questions may be decided by the administrative body, reserving others for the courts.

In Armour & Co. v. Alton R. R. Co., 312 U. S. 195, 85 L. Ed. 771, a shipper sued to eliminate the yardage charge necessitated by the delivery by the carrier other than to the consignee. The court, in holding that prior resort to the Commission was essential, stated:

> "The complexities of the situation here presented are graphically illustrated in the companion case of Swift & Co. v. Alton R. Co., 238 Inters. Comm. Rap. 179. Swift, one of Armour's competitors, took its petition for alteration of the same long standing practice to the Commission. That expert body found it a necessary prerequisite decision to have a trial examiner

conduct extensive hearings, compiling in the process a record of 5 volumes, 1,147 pages and numerous exhibits."

All of the foregoing cases reiterate the principle with which Corneli agrees, that is, questions presenting complex issues within the administrative expertise should be decided by the Commission, while questions of simple tariff constructions may be passed on by the courts as questions of law.

We next examine cases cited by Union Pacific for the proposition that when primary Commission jurisdiction is present the Commission finding is only subject to review. As we have pointed out, Terminal Warehouse Co. v. Pennsylvania R. R. Co., discussed above, is no longer authority for the proposition that in such a case judicial inquiry is foreclosed respecting a negative finding by the Commission, this proposition having been expressly overruled in the case of United States v. Interstate Commerce Commission, supra. In the latter case the sole issue before the court was the reviewability of a dismissal of a shipper's complaint before the Commission after a finding of no damages, and the action was held to be reviewable.

The case of Johnson Seed Company v. United States (10th Cir. 1951), 191 F. 2d 228, is a typical reasonableness of rates case and involved the review of a determination by the Commission that a certain rate was reasonable in its application to certain shipments of seed. The determination by the Commission was within its primary jurisdiction, and its determination when supported by evidence was binding on the court.

Both the cases of Interstate Commerce Commission v. Martin Box Brothers Co., 219 F. 2d 811 (9th Cir.), and Shipper's Car Supply Commission v. Interstate Commerce Commission, 160 F. Supp. 939 (D. C. Or. 1958), deal with the question of the reasonableness of the carrier in refusing to provide boxcars as specifically provided by the In-

terstate Commerce Act. In stating that the findings of fact of the Commission as to the unreasonable refusal by the carriers are subject to limited review, the courts noted the reluctance of the judiciary to disturb such findings in such cases. However, these cases have absolutely no bearing on the case at bar in that they are not concerned with the construction of a tariff provision on disputed facts, and they are in substance dealing with complex issues, particularly within the Commission's jurisdiction. The case of New Process Gear Corporation v. New York Central R. Co., 250 F. 2d 569, is distinguishable on the same grounds.

The case of Reliance Steel Products Co. v. United States, 150 F. Supp. 118, holds that where primary jurisdiction is present and a negative order is involved that limited review only is available. This is, of course, true in this case respecting the denial of Corneli's application for the establishment of routes and rates and also as to the reasonableness of the combined and transit rates, but the case does not decide that in an admitted fact situation with a question of law involved that the courts are confined to limited review. In the latter situation Great Northern applies and the Commission determination is not conclusive as is pointed out in Baltimore & Ohio v. Owens, supra.

Two cases are cited in support of the argument that Corneli is estopped to assert that the Commission's dismissal order is not conclusive. The first, Callanan Road Improvement Co. v. United States, 345 U. S. 507, 97 L. Ed. 1206, involved a situation where Callanan had acquired an existing certificate of convenience and necessity for operation as a common carrier in New York Harbor and adjacent waters. At the time of transfer the certificate was restricted to freightage. Subsequent to the acceptance of the transfer and operation under it Callanan asked the Commission to construe his certificate to include both freightage and towage. The Commission denied relief. The Supreme Court held on appeal that by having accepted

the certificate limited as it was to freightage and having operated under it for several years, that Callanan was estopped to assert to the contrary, and that the limitation to freightage should have been attacked before the Commission at the time of its approval of the transfer. In other words, Callanan had taken an inconsistent position by acquiescing in the Commission's interpretation and later sought a contrary interpretation. Corneli has at all times adhered to but one position in this case, namely, that the transit rates apply to transit cargo. Therefore, this case has no applicability whatsoever. Furthermore, in Brown & Sons Lumber Co. v. Louisville & N. R. Co., 299 U. S. 393, 81 L. Ed. 301, the carriers had contended for a particular interpretation of a tariff before the Commission and the holding was adverse to their contention. In a subsequent suit by the shippers on the award of the Commission of reparations to the shipper the Supreme Court expressly held that the carriers were not estopped from maintaining the same interpretation that they urged before the Commission, although they had not appealed from an adverse result. The court further sustained the construction of the carriers and said, l. c. 81 L. Ed. 304, "We so hold despite the construction given the rule by the Commission." The Brown case completely destroys the position of Union Pacific with respect to any argument based on estoppel.

The case of Elbow Lake Coop. Grain Co. v. Commodity Credit Corporation, 144 F. Supp. 54, was an action by grain warehousemen for a determination of the quality and quantity of grain under United States Grain Standards Act wherein the court held that the failure to exhaust administrative remedies would preclude the initiation of an action by the grain warehousemen to determine such quality and quantity. This case is not in point because as expressly held in the Western Pacific case the failure to exhaust administrative remedies has no application to the doctrine of primary jurisdiction.

The foregoing should suffice to demonstrate that the authorities do not support Union Pacific's contention as to the conclusiveness of the Commission's report.

II.

We come now to consider Union Pacific's second question presented which is stated to be that Union Pacific could not waive or condone a practice not authorized by the tariff. As heretofore stated, Corneli is in full agreement with this principle, but the question remains whether or not the furnishing of inbound references after shipment was a compliance with the transit tariff respecting admittedly transit shipments. Corneli submits that such was the case under the admitted facts and law, as has been fully expounded in Corneli's original brief.

Union Pacific cites many cryptic quotations supporting its general proposition, however, it may be helpful to consider the context in which the statements were made. Considering first the statement of this court in National Carloading Corporation v. Atchison, Topeka & Santa Fe Railway Company (9th Cir. 1955), 150 F. 2d 210, to the effect that conduct, intention, mistake and misunderstanding are no defense to an action by a carrier for undercharges. Examining the opinion discloses that the shipper made it a practice to demand a 50 foot car, and induced the carrier to furnish two 40 foot cars. The record shows that there was a collusive agreement, plan and understanding, and a clear violation of the tariff which could not have been for the "carrier's convenience" which if so would have made the substitution permissible under the tariff. Clearly here the carrier got an illegal preference and discrimination. In West Coast Products Corporation v. Southern Pacific Company (9th Cir. 1955), 226 F. 2d 830, two classifications were available for the shipment of olives, one applicable to salt cured olives not preserved in liquid, and the other applicable to olives preserved in liquid. This

court held the olives were salt cured, and that the liquid tariff did not apply. During the course of the opinion the court notes that it had been suggested that some prior shipments had been given the preserved in liquid classification but holds that since the carrier was not subject to estoppel that improper application of the past were no defense to the application of the appropriate rate. This case has no application for the reason that the admitted facts in this case show that at all times past, present and future, Corneli's cargo was, in fact, transit cargo and entitled to transit rates.

In Northern Pacific Railway Company v. Mackie (9th Cir. 1952), 195 F. 2d 641, this court had before it an action against Northern Pacific for damages to a carload of plywood, the defense being failure to file a written claim within the 9 months period. The evidence was that there had been verbal notices, but it is held that the written notice was a condition precedent to recovery, non-compliance with which would open the door to evasion. This class of case is distinguishable from the situation at bar because the giving of written notice of a claim as a condition precedent to recovery creates a statutory bar to the cause of action. Not so in determining when data is to be furnished to secure a transit rate. Any precedent condition can as well be satisfied at the time of a shipment or a short time thereafter so long as the privileged rate is not granted until the data is at hand.

In the case of Frank O. Lowden v. Simonds-Shields-Lonsdale Grain Co., 306 U. S. 516, 83 L. Ed. 953, the railroad sued for services rendered in the installation of grain doors, such charge being authorized by the tariff. Before the trial in the District Court the Commission considered the reasonableness of the charge, reducing a charge of a dollar to sixty cents per car. The shippers advised the carriers they would not pay, but demanded that shippers furnish coopered cars. The court held that the railroad

could collect the charge because it was required by the terms of the tariff, notwithstanding shippers' attempt to disclaim liability. This case is cited for the proposition that the court should aid carriers in collecting published charges. We agree.

In Louisville & Nashville Railroad Company v. Maxwell, 237 U. S. 94, 59 L. Ed. 853, the railroad sued a passenger to recover an alleged undercharge. The defense was that there was no undercharge because the passenger could have made the same trip by a different route at the price paid. This defense was rejected because of the fact that the passenger had selected the route, and the availability of other routes was held not to be a defense. Because the court said so long as the proper tariff was not paid for the route selected the carrier must recover the difference. No such question of routes is involved in the case at bar. In Armour & Company v. Atchison, Topeka & Santa Fe Railroad Company (7th Cir. 1958), 254 F. 2d 719, Armour & Company sued the carriers for overcharges by reason of the fact that the aggregate local rates were less than through rates. The action was brought under 49 U. S. C. A., Section 16 (2), reparations having been awarded by the Commission. The railroads defended on the ground that the aggregate rates erroneously included a particular basing point and the rates therefrom when in fact the station had been abandoned, but the railroads had not amended their tariffs to so show. The court held that the published rates were applicable and affirmed a judgment in favor of the shipper against the carrier. During the course of the opinion the court says that the legality of the rate was not dependent upon equities involved, namely the failure of the railroad to amend its tariff. The court also held, however, that the proof did not show the basing point station had been abandoned. In the case at bar no question of amending a tariff is involved. It is stipulated that the combination rates, which the Union Pacific seeks to

collect in this case, are in excess of the transit rate. Therefore, the only question is as to the application of the transit rate.

The cases of Oregon, Washington R. & Nav. Co. v. C. M. Kopp Co. (Wash.), 120 P. 2d 845, 138 A. L. R. 633; Chicago & Alton R. R. v. Kirby, 225 U. S. 155, 56 L. Ed. 1033, and Davis v. Cornwell, 264 U. S. 560, 68 L. Ed. 848, all deal with the question of whether a shipper may recover against a carrier on an agreement to furnish extra services not specified in the transit tariff. These cases are in accord with the general rule that a shipper may not recover against a carrier for a breach of an agreement for extra services not covered under the terms of the tariff. Union Pacific argues that this rule is applicable because the handling of the information which was furnished by Corneli under the claim procedure involved some kind of extra service which would amount to a discrimination in Corneli's favor. Corneli is not seeking anything from the railroad for alleged services which Corneli rendered, and it is submitted that the railroad, whether it received the inbound reference on the outbound bill of lading or later at the time it applied the transit tariff, had only the same so-called service to perform which would consist merely of debiting the tonnage credit with the tonnage of the outbound cargo. In addition, Union Pacific suggests that once the outbound shipment had been made it could no longer determine whether the shipment was entitled to transit privileges. This is an unsupportable contention in view of the fact that the Union Pacific has stipulated that when the claim information had been completed that Corneli's admittedly outbound cargo had applied to it the proper through transit rate. To argue that Union Pacific could not do something that it had done for a period of many years belies the admitted facts in the record. In the Oregon, Washington Railroad case the carrier sued the shipper for transportation charges and was met with a

counterclaim for damages on account of the alleged negligent delay in the transportation of lettuce based upon the failure of the carrier to give notice to the shipper of the accomplishment of a diversion order, in accordance with an alleged custom and practice of the carrier not published in its tariff. Recovery was denied the shipper for the reason that it involved an additional service to the shipper with respect to which a charge could not be exacted unless published. The court therefore held that failure to perform the custom gave no cause of action to the shipper. Corneli submits that there is no question of custom in this case in the sense that the term is used in the cases involving so-called customs and practices as constituting the extension of privileges or facilities to shippers. Davis v. Cornwell dealt with an alleged agreement to furnish a car on a certain day. The Chicago & Alton case was an action by shipper of horses against a carrier on an alleged special contract to give fast delivery to a connecting carrier so as to effect a speedy arrival of the horses at destination. Davis v. Henderson, 266 U. S. 92, 69 L. Ed. 182, was a suit by a shipper for damages for failure to furnish a railroad car, although the shipper had not complied with the requirement of the tariff that the order should have been in writing. This is the classic case on precedent conditions and the strict application thereof in tariff cases. Like the notice provisions in claim cases the principle is invoked to defeat actions brought to recover damages against carriers. There is not involved the question of the application of a lawful tariff when there is a question of which of two tariffs are applicable. The foregoing should suffice to show that this line of cases has no bearing on the issue in this case. One searches in vain for any case cited by Union Pacific which can be said to be controlling in the case here before this court, although as stated at the outset all support the general proposition of Union Pacific's second question presented.

SUMMARY.

To summarize, we think it may be fairly said that Union Pacific's position is that under the doctrine of primary jurisdiction the construction of the transit tariff and whether or not there was compliance with it was a matter within the special competence of the Interstate Commerce Commission, and within the case of United States v. Western Pacific rule, and such being the case the Commission decision is conclusive. Opposed to this Corneli's position is that the construction and application of the tariff was not a question within United States v. Western Pacific's rule, but rather a question within the rule of Great Northern Railway v. Merchant's Elevator Company, supra, in which event a question of law is presented and the decision of the Interstate Commerce Commission is not immune from judicial inquiry. On the construction question Union Pacific asserts that the furnishing of the in-transit data was a precedent condition so as to require the data on the outbound bill of lading, whereas Corneli asserts that so long as the in-transit information was submitted prior to the application of the transit rate, the conditions of the tariff precedent or otherwise were complied with, and the application of the transit rate to the admittedly transit cargo would be the lawful application of the proper rate as required by all of the cases, whereas the application of the combined rate would be the application of an unlawful rate to admittedly transit shipments.

As stated in our original brief, any decision of this court which would apply combination rates to admittedly transit shipments would constitute a triumph of technicality over justice. This is not a plea for equitable considerations, but rather a plea that a reasonable construction be given to the application of the tariff in conformance with what the parties themselves consider to be an appropriate and reasonable construction. The suggestion of Union Pacific that

Corneli in this case engaged on a policy of deliberate evasion of the tariff presupposes that Union Pacific and Corneli were engaged in some sort of illegal and unauthorized conduct when such is not the case. On this record Union Pacific and Corneli were in good faith attempting to comply with the tariff by applying through transit rates to through transit shipments. A decision of this court so holding is respectfully requested.

Respectfully submitted,

FORREST M. HEMKER,
GREENSFELDER, HEMKER & WIESE,
705 Olive Street,
St. Louis 1, Missouri,
Attorneys for Corneli Seed Company,
Appellant.

I certify that on the 13th day of November, 1958, I served three full, true and correct copies of the foregoing brief upon the plaintiff (appellee) by enclosing a copy in an envelope addressed to plaintiff's (appellee's) attorney as follows: Mr. L. H. Anderson, General Attorney, Union Pacific Railroad Company, Carlson Building, P. O. Box 530, Pocatello, Idaho, that being his last known address, and depositing the same, postage prepaid, in the United States Post Office at St. Louis, Missouri.

.....
Counsel for Appellant.

Subscribed and sworn to before me this 13th day of November, 1958.

.....
Notary Public.

My term expires:

No. 16109

United States Court of Appeals

for the Ninth Circuit

MARGARET LILLIAN FERGUSON, NEWTON IVAN SHERRY and LOIS SHERRY,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Petition to Review Decisions of The Tax Court of the United States

FILED
OCT - 1 1958
PAUL P. O'BRIEN, CLERK

Phillips & Van Orden Co., Fourth and Berry Sts., San Francisco, Calif.—9-19-58

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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The Tax Court of the United States

Docket No. 56085

MARGARET LILLIAN FERGUSON,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

1955

Jan. 24—Petition received and filed. Taxpayer notified. Fee paid.

Jan. 26—Copy of petition served on General Counsel.

Jan. 24—Request for Circuit hearing in Los Angeles, Calif. filed by taxpayer. 2/2/55—Granted.

Mar. 15—Answer filed by General Counsel.

Mar. 21—Copy of answer served on taxpayer, Los Angeles, Calif.

May 2—Reply to answer filed by taxpayer. Copy served.

1956

Oct. 19—Hearing set Jan. 7, 1957—Los Angeles, Calif.

Dec. 19—Motion to continue to the next Los Angeles calendar, filed by petitioner, 12/20/-56—Granted.

Dec. 21—Motion Served.

1957

Feb. 20—Hearing set Apr. 15, 1957—Los Angeles, Calif.

Apr. 15—Trial had before Judge Raum on joint oral motion to consolidate with 56086 for trial—Granted. Stipulation of facts filed at Hearing, Petitioner's Brief due 5/31/-57; Respondent's Brief due 7/1/57; Petitioner's Reply Brief due 7/22/57.

May 8—Transcript of Hearing 4/15/57 filed.

May 31—Brief filed by Petitioner. Served 5/31/57.

Jun. 28—Respondent's Brief in answer filed. 7/2/-57 served.

July 19—Petitioner's Reply Brief filed. Served 7/22/57.

1958

Feb. 26—Memo. Findings of Fact and Opinion filed, Judge Raum, Decision under R. 50. Served 2/26/58.

May 14—Agreed computation filed.

May 19—Decision entered, Judge Raum.

Jun. 16—Petition for Review by U. S. Ct. of Ap. 9th Cir. filed by petitioner.

Jun. 16—Designation of contents of record on review filed.

Jun. 16—Proof of service of petition for review and designation filed.

The Tax Court of the United States

Docket No. 56086

NEWTON IVAN SHERRY, LOIS SHERRY,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

[Note: Docket Entries for case No. 56086 are a duplication of Docket Entries for case No. 56085.]

[Title of Tax Court and Cause No. 56085.]

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency dated October 28, 1954, and as a basis of her proceeding alleges as follows:

1. Petitioner is an individual with residence at 1810 Courtney Avenue, Los Angeles 46, California. The returns for the years here involved were filed with the Collector at Los Angeles, California.

2. The Commissioner has addressed the statutory notice to petitioner as "Mrs. Robert W. Ferguson (formerly Margaret Lillian Sherry)." Although petitioner is married to Robert W. Ferguson, her

correct name is Margaret Lillian Ferguson, and this petition is filed under the latter name.

3. The notice of deficiency (a copy of which is attached and marked Exhibit "A") was mailed to the petitioner on October 28, 1954.

4. The deficiency as determined by the Commissioner is in income taxes as follows:

Year	Deficiency	50% Penalty
1944	$ 5,817.27	$ 2,908.63
1945	5,124.55	3,117.15
1946	45,333.52	22,666.76
	$56,275.34	$28,692.54

All of the above tax deficiencies and penalties are in controversy.

5. The determination of tax set forth in said notice of deficiency is based upon the following errors:

(a) The Commissioner has erroneously determined said deficiencies and penalties because the statute of limitations under Section 275 of the Internal Revenue Code of 1939 has run on all of the above years;

(b) The Commissioner has erroneously determined that an alleged partnership called Sherry Enterprises existed and that petitioner was a partner therein;

(c) The Commissioner has erroneously determined that the increase in net worth of said alleged partnership was the result of income received by such partnership;

(d) The Commissioner has erroneously used the "net worth" method to determine said deficiencies;

(e) The Commissioner has erroneously determined that petitioner received income from said alleged partnership during said years; and

(f) The Commissioner has erroneously added fraud penalties to said deficiencies. There was no intent to evade payment of income taxes.

6. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) Petitioner's income tax returns for the above years were filed with said Collector on or before the following dates:

1944—March 15, 1945.
1945—March 15, 1946.
1946—March 16, 1947.

The statute of limitations (section 275 of the Internal Revenue Code of 1939) has run, therefore, on all of the above years.

(b) Petitioner was not a partner in any partnership known as Sherry Enterprises because there was, in fact, no such partnership. But even if this Court should determine that such partnership did exist, petitioner was not a partner therein. Petitioner was on active duty with the United States Navy from February, 1943, to November, 1945, and from February, 1946, to June, 1946, she attended the University of Southern California. Petitioner did not participate in the transactions or businesses involving the alleged Sherry Enterprises during any of the above taxable years. She also did not

receive any money or property from the alleged partnership during any of said years, either as the income of such partnership or otherwise.

(c) If it should be determined that such alleged partnership did exist, petitioner alleges that the partnership kept adequate books and records during said years which clearly reflect its income. Hence the Commissioner erroneously reconstructed the income of the alleged partnership by using the "net worth" method.

(d) Further, that in the event this Court determines that such alleged partnership did exist during the above years and that petitioner was a partner therein, petitioner alleges that the increase in net worth of such partnership over and above the income reported by the partnership in its tax returns was the result of capital contributions by Nathan Sherry, the deceased father of petitioner, and not as the result of income earned or received by the partnership. During said years Nathan Sherry made the following capital contributions to the alleged partnership:

	Fiscal Years Ending		
	6-30-44	6-30-45	6-30-46
Cash	$ 74,663.60	$ 4,348.00	$ 42,000.00
Bonds	5,000.00	5,000.00	40,000.00
Interest in partnerships		4,572.50	62,211.50
Cashier's checks			60,000.00
Real Estate		17,500.00	3,000.00
Notes and Accounts Receivable			5,000.00
Furniture and Fixtures			2,120.00
Other			30,000.00
Totals	$ 79,663.60	$31,420.50	$244,331.50

Also, the Commissioner has erroneously included as an accounts receivable of the alleged partnership on June 30, 1946, the amount of $30,000.00 as an accounts receivable due from Edward J. Margett. Edward J. Margett did not owe the alleged partnership the sum of $30,000.00 or any other amount on June 30, 1946.

Wherefore, the petitioner prays that this Court may hear the proceedings and determine that there is no deficiency due from the petitioner for the years 1944 to 1946, inclusive.

/s/ CHARLES H. CARR
/s/ WILLIAM K. RASMUSSEN,
Counsel for Petitioner

Duly Verified.

EXHIBIT "A"

1250 Subway Terminal Building, 417 South Hill Street, Los Angeles 13, California

Ap:LA:AA:PAK
90D. Oct. 28, 1954

Mrs. Robert W. Ferguson
(Formerly Margaret Lillian Sherry)
1810 Courtney Street, Los Angeles, California

Dear Mrs. Ferguson:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1944, December 31, 1945, and December 31, 1946 discloses deficiencies in tax aggregating $56,275.34 and penalties aggregating $28,692.54, as shown in the statement attached.

Exhibit "A"—(Continued)

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiencies mentioned.

Within 90 days from the date of mailing of this letter you may file a petition with The Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday, or legal holiday in the District of Columbia, in which event that day is not counted as the 90th day. Otherwise Saturdays, Sundays, and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute, in duplicate, the enclosed form and forward it to the Assistant Regional Commissioner, Appellate, 1250 Subway Terminal Building, 417 South Hill Street, Los Angeles 13, California. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment, whichever is earliest.

Very truly yours,

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue
/s/ By W. T. TIGNOR,
Associate Chief, Appellate Division

Exhibit "A"—(Continued)

Enclosures: Statement, Form 1276, Agreement Form.

PAKar:lee 10/8/54

Statement

Ap:LA:AA-PAK

Mrs. Robert W. Ferguson (formerly Margaret Lillian Sherry), 1810 Courtney Street, Los Angeles, California

Tax Liability for the Taxable Years Ended December 31, 1944, to December 31, 1946, Inclusive

Year		Deficiency	50% Penalty
1944	Income tax	$ 5,817.27	$ 2,908.63
1945	Income tax	5,124.55	3,117.15
1946	Income tax	45,333.52	22,666.76
	Total	$56,275.34	$28,692.54

In making this determination of your income tax and penalty liability careful consideration has been given to the report of examination dated November 24, 1952, to your protest dated February 24, 1953, and to the statements made at hearings held on January 27, 1954 and July 16, 1954.

The 50 percent penalty has been asserted for each of the taxable years 1944, 1945, and 1946 under the provisions of section 293(d) of the Internal Revenue Code of 1939.

The deficiency for the year 1944 is assessable under the provisions of section 276(a) of the Internal Revenue Code of 1939.

The deficiencies for 1945 are assessable under the provisions of section 275(c) and 276 of the Internal Revenue Code of 1939.

It has been determined that your share of the distributable income from the Sherry Enterprises partnership is $23,940.84 for 1944, $29,889.98 for 1945, and $82,742.97 for 1946. Inasmuch as you reported $13,100.14 in 1944, $21,841.88 in 1945, and $14,792.91 in 1946, your taxable income has been increased by the differences of $10,840.70, $8,048.10, and $67,950.06, respectively, computed as follows:

Exhibit "A"—(Continued)

COMPUTATION OF NET WORTH OF PARTNERSHIP

Assets	Oct. 1, 1943	Jun. 30, 1944	Jun. 30, 1945	Jun. 30, 1946
Cash	$12,094.96	$ 10,322.24	($ 363.71)	$ 28,176.59
Stocks	5,997.88	.....	.....	.....
Bonds	.....	50,000.00	50,000.00	50,000.00
Interest in partnership	49,577.70	90,712.18	133,424.34	348,326.34
Cashier's checks	.....	.....	2,000.00	60,000.00
Real estate	.....	.....	118,020.42	94,619.50
Notes and accounts receivable	.....	50,000.00	30,000.00	42,400.00
Furniture and fixtures	.....	.....	.....	6,743.55
Total Assets	$67,670.54	$201,034.42	$333,081.05	$630,265.98
Liabilities:				
Accounts payable	$ 5,000.00	$ 403.34	$	$ 15,000.00
Notes payable	.....	45,000.00	40,000.00	.....
Trust deed payable	.....	.....	21,400.00	17,500.00
Total Liabilities	$ 5,000.00	$ 45,403.34	$ 61,400.00	$ 32,500.00
Net Worth	$62,670.54	$155,631.08	$271,681.05	$597,765.98

	1944	1945	1946
Net worth at end of year	$155,631.08	$271,681.05	$597,765.98
Net worth at beginning of year	62,670.54	155,631.08	271,681.05
Increase in net worth	$ 92,960.54	$116,049.97	$326,084.93
Additions:			
Personal expenses	1,248.14	6,883.00	12,127.62
Federal income tax payments	6,486.08	23,324.89	22,397.86
State income tax payments	.....	573.70	.....
Payment to stock brokers	10,000.00	900.00	1,915.00
Purchase of personal items	.....	.....	6,911.01
Total	$110,694.76	$147,731.56	$369,436.42
Reductions:			
Proceeds of sale of auto	1,500.00	.....	.....
Proceeds of sale of stock	.....	2,498.50	.....

Exhibit "A"—(Continued)

	1944	1945	1946
Capital contributions	.....	12,040.00	5,000.00
Earnings prior to Oct. 1, 1943	13,431.40	.....	.....
Check from brokers	.....	10,614.31	.....
Balance	$ 95,763.36	$122,578.75	$364,436.42
Add: Income adjustments:			
Ordinary income of partnership	.....	.....	1,170.00
Short-term capital gain	.....	(5,000.00)	(277.00)
Long-term capital gain—taxable portion	.....	(3,989.17)	(17,178.78)
Long-term capital gain—nontaxable portion	.....	(3,989.17)	(17,178.78)
Ordinary net income corrected	$ 95,763.36	$109,600.41	$330,971.86
Ordinary net income per return	52,400.54	77,407.99	59,171.64
Understatement of net income	$ 43,362.82	$ 32,192.42	$271,800.22
Your distributive share of amount of understatement	$ 10,840.70	$ 8,048.10	$ 67,950.06

A copy of this letter and statement has been mailed to your representative, Mr. Charles H. Carr, 417 South Hill Street, Los Angeles 13, California, in accordance with the authority contained in the power of attorney executed by you.

Taxable Year Ended December 31, 1944

ADJUSTMENT TO NET INCOME

Net income as disclosed by return	$ 12,600.13
Additional income:	
(a) Income from partnership	10,840.70
Net income adjusted	$ 23,440.83

EXPLANATION OF ADJUSTMENT

(a) This adjustment is previously explained herein.

COMPUTATION OF TAX

Net income adjusted	$ 23,440.83
Less: Surtax exemption	500.00
Surtax net income	$ 22,940.83

Exhibit "A"—(Continued)

Net income adjusted	$ 23,440.83	
Less: Normal tax exemption	500.00	
Net income subject to normal tax	$ 22,940.83	
Normal tax at 3% of $22,940.83		$ 688.23
Surtax on $22,940.83		8,935.10
Total normal tax and surtax		$ 9,623.33
Correct income tax liability		$ 9,623.33
Income tax liability shown by return, Account No. 9016323		3,806.06
Deficiency of income tax		$ 5,817.27
50 percent penalty		2,908.63

Taxable Year Ended December 31, 1945

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return	$ 21,449.28
Additional income:	
(a) Income from partnerships	10,537.98
Total	$ 31,987.26
Reductions:	
(b) Long-term capital gain	742.15
Net income adjusted	$ 31,245.11

EXPLANATION OF ADJUSTMENTS

(a) Income from partnerships is increased by $10,537.98 consisting of the following:

(1) Income from Sherry Enterprises (partnership)	$ 8,048.10
(2) Income from other partnerships	2,489.88
Total	$ 10,537.98

(1) This adjustment is previously explained herein.

(2) This adjustment was previously made to net income and agreed to by you.

(b) This adjustment was previously made to net income and agreed to by you.

Exhibit "A"—(Continued)

COMPUTATION OF ALTERNATIVE TAX

Net income adjusted		$ 31,245.11
Less: Excess of net long-term capital gain over net short-term capital loss		255.14
Ordinary income		$ 30,989.97
Less: Surtax exemption		500.00
Surtax net income		$ 30,489.97
Ordinary net income	$ 30,989.97	
Less: Normal-tax exemption	500.00	
Balance subject to normal tax	$ 30,489.97	
Normal tax at 3% of $30,489.97		$ 914.70
Surtax on $30,489.97		13,523.79
Partial tax		$ 14,438.49
Plus: 50% of $255.14		127.57
Alternative tax		$ 14,566.06

COMPUTATION OF TAX

Net income adjusted		$ 31,245.11
Less: Surtax exemption		500.00
Balance subject to surtax		$ 30,745.11
Net income adjusted	$ 31,245.11	
Less: Normal-tax exemption	500.00	
Net income subject to normal tax	$30,745.11	
Normal tax at 3% of $30,745.11		$ 922.35
Surtax on $30,745.11		13,681.97
Total normal tax and surtax		$ 14,604.32
Alternative tax		$ 14,566.06
Correct income tax liability		$ 14,566.06
Income tax liability shown on return,		
Account No. 3040632	$ 8,331.76	
Additional, Oct. 1, 1948, No. 10-510047	1,109.75	9,441.51
Deficiency of income tax		$ 5,124.55

Exhibit "A"—(Continued)

50% penalty:

Correct income tax liability	$14,566.06	
Liability shown by return	8,331.76	
Excess	$ 6,234.30	
50% penalty (50% of $6,234.30)		$ 3,117.15

Taxable Year Ended December 31, 1946

ADJUSTMENT TO NET INCOME

Net income as disclosed by return	$ 18,656.85
Additional income:	
(a) Income from partnership	67,950.06
Net income adjusted	$ 86,606.91

EXPLANATION OF ADJUSTMENT

(a) This adjustment has been previously explained herein.

COMPUTATION OF ALTERNATIVE TAX

Net income adjusted		$ 86,606.91
Less: Excess of net long-term capital gain over net short-term capital loss		4,294.70
Ordinary net income		$ 82,312.21
Less: Exemption		500.00
Balance, subject to surtax and normal tax		$ 81,812.21
Tentative surtax	$ 49,287.89	
Tentative normal tax at 3%	2,454.36	
Total tentative tax	$ 51,742.25	
Less 5%	2,587.11	
Partial tax		$ 49,155.14
Plus: 50 percent of $4,294.70		2,147.35
Alternative tax		$ 51,302.49

COMPUTATION OF TAX

Net income adjusted	$ 86,606.91
Less: Exemption	500.00
Balance, subject to surtax and normal tax	$ 86,106.91

Exhibit "A"—(Continued)

Tentative surtax	$ 52,766.60	
Tentative normal tax at 3%	2,583.20	
Total tentative tax	$ 55,349.80	
Less 5%	2,767.49	
Total normal tax and surtax		$ 52,582.31
Alternative tax		$ 51,302.49
Correct income tax liability		$ 51,302.49
Income tax liability shown on return, Account No. 3036202		$ 5,968.97
Deficiency of income tax		$ 45,333.52
50% penalty		$ 22,666.76

[Endorsed]: T.C.U.S. Filed January 24, 1955.

[Title of Tax Court and Cause No. 56085.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, R. P. Hertzog, Acting Chief Counsel, Internal Revenue Service, for answer to the petition of the above-named taxpayer, admits, denies and alleges as follows:

1, 2, 3, 4. Admits the allegations contained in paragraphs 1, 2, 3, and 4 of the petition.

5. Denies the allegations of error contained in paragraph 5 of the petition, and all subparagraphs thereof.

6. (a) Denies the allegations of subparagraph (a) of paragraph 6 of the petition; avers that petitioner's income tax returns for the years 1945 and 1946

were filed with said Collector on March 15, 1946 and March 15, 1947, respectively.

(b), (c), (d). Denies the allegations contained in subparagraphs (b), (c), and (d) of paragraph 6 of the petition.

7. Denies generally and specifically each and every allegation contained in the petition, not hereinbefore specifically admitted, qualified or denied.

Further answering the petition, the respondent alleges that:

8. The petitioner is liable for the fifty percent fraud penalties proposed under Section 293(b) of the Internal Revenue Code of 1939 for the taxable years 1944, 1945 and 1946 in the respective amounts of $2,908.63, $3,117.15, and $22,666.76 as determined by the Commissioner and set forth in his notice of deficiency. In support of the Commissioner's determination of such fraud penalties, the respondent alleges and relies upon the following facts:

(a) That petitioner caused to be prepared and filed with the Collector of Internal Revenue for the Sixth District of California individual income tax returns for the taxable years 1944, 1945 and 1946 and represented that each such return was a true, correct return.

(b) In truth and in fact, each of the said returns filed by the petitioner for the taxable years 1944, 1945 and 1946 was false and fraudulent in that they understated the true and correct amounts of net income and resultant tax liability thereon for each of such taxable years. The extent of the false and

fraudulent understatement of net income and income tax liability for each of such years is as follows:

Year	Net Income Reported	Tax Liability Reported	Correct Net Income	Correct Tax Liability
1944	$12,600.13	$3,806.06	$23,440.83	$ 9,623.33
1945	21,449.28	8,331.76	31,245.11	14,566.06
1946	18,656.85	5,968.97	86,606.91	51,302.49

(c) At the time the aforesaid returns for the taxable years 1944, 1945 and 1946 were prepared and filed, the petitioner knew that such returns were false and fraudulent, and that the amount of net income reported therein and the resultant tax liability shown thereon were understated in each of the said returns. The petitioner knowingly, wilfully and fraudulently made and filed her income tax returns for the taxable years 1944, 1945 and 1946 with intent to deceive respondent and evade tax.

(d) During the taxable years in question, petitioner derived and received income from partnership operations conducted under the partnership name of Sherry Enterprises.

(e) Books and records pertaining to the income producing activities of the aforementioned partnership during the years in question were too inadequate and insufficient to enable the Commissioner, through his examining agents, to check and verify the partnership's correct net income and petitioner's share thereof for the taxable years 1944, 1945 and 1946; said records were inadequate in that they were incomplete as to some of the partnership's income producing activities and no records were kept of other partnership income producing ac-

tivities. Consequently, it became necessary for the Commissioner to determine the correct amounts of taxable net income for the years involved from other sources of information. The Commissioner, through his examining and investigating agents, determined the taxable income of the partnership for such years by the "Net Worth and Expenditures Method."

(f) The corrected income of the partnership and the petitioner's share thereof is determined for the taxable years 1944, 1945 and 1946 by reference to the increase in net worth of the partnership during such years, as shown in Exhibit 1 attached to this answer and incorporated herein by reference.

(g) The understatement of petitioner's income and income tax liability for each of the taxable years 1944, 1945 and 1946 was due to fraud with intent to evade tax.

(h) Petitioner having filed false and fraudulent returns with intent to evade tax for the taxable years 1944, 1945 and 1946, neither the assessment nor collection of the proposed deficiencies is barred by any statute of limitations under the provisions of Section 276(a) of the Internal Revenue Code of 1939.

9. Further answering the petition, for an alternative defense, respondent alleges that the five-year period of limitation is applicable under Section 275(c) of the Internal Revenue Code of 1939 for assessment and collection of the deficiency determined by the Commissioner for the taxable year 1945 as set forth in the notice of deficiency. In sup-

port of such determination, respondent alleges as follows:

(a) On March 15, 1946 petitioner filed her return for the year 1945 with the Collector of Internal Revenue for the Sixth District of California.

(b) Petitioner improperly omitted from gross income reported for the year 1945 an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return.

(c) On December 14, 1950, and within five years after filing petitioner's income tax return for 1945, the petitioner and the Commissioner duly executed a waiver consenting to the assessment and collection of any deficiency which might be determined for the year 1945 predicated upon the Commissioner's proper inclusion in petitioner's gross income of an amount in excess of 25 percent of the gross income stated in her return and the application of the five-year statutory period of limitation as provided under Section 275(c) of the Internal Revenue Code. Successive agreements were later timely executed by petitioner and respondent, further extending the statute of limitations until June 30, 1955 with respect to such taxable year. Respondent's notice of deficiency mailed to petitioner on October 28, 1954 was timely mailed under the provisions of Sections 275(c) and 276(b) of the Internal Revenue Code of 1939.

10. Further answering the petition, respondent alleges as follows:

(a) On March 15, 1947 petitioner filed her return

for the year 1946 with the Collector of Internal Revenue for the Sixth District of California. On March 6, 1950, and before the expiration of the three-year statute of limitations with respect to the year 1946, the petitioner and the Commissioner duly executed a waiver extending the statute of limitations. Successive agreements were later timely executed by petitioner and respondent, further extending the statute of limitations until June 30, 1955 with respect to such taxable year. Respondent's notice of deficiency mailed to petitioner on October 28, 1954 was timely mailed under the provisions of Section 276(b) of the Internal Revenue Code of 1939.

Wherefore, it is prayed:

1. That the relief sought in the petition be denied.

2. That the deficiencies in income taxes for the taxable years 1944, 1945 and 1946, as set forth in the notice of deficiency, be in all respects approved.

3. That the deficiencies in fraud penalties for the taxable years 1944, 1945 and 1946, as set forth in the notice of deficiency, be in all respects approved.

4. That this Court find and hold that the assessment and collection of the proposed deficiencies for the taxable years 1944, 1945 and 1946 are not barred by any statute of limitations under the provisions of section 276(a) of the Internal Revenue Code for 1939.

5. In the alternative, that this Court enter its decision that petitioner improperly omitted from gross income reported for the year 1945 an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in such return; that for the year 1945 the five-year period of limitation for assessment and collection of the income tax deficiency for such year attaches pursuant to Section 275(c) of the Internal Revenue Code for 1939; that the Commissioner's notice of deficiency mailed to petitioner on October 28, 1954 was timely under the provisions of sections 275(c) and 276(b) of the Internal Revenue Code of 1939; and that the assessment and collection of the deficiencies for the years 1945 and 1946 is not barred.

/s/ R. P. HERTZOG, ECC.
Acting Chief Counsel, Internal Revenue Service

Of Counsel: Melvin L. Sears, Regional Counsel, E. C. Crouter, Assistant Regional Counsel, R. E. Maiden, Jr., Special Assistant to the Regional Counsel, Mark Townsend, Attorney, Internal Revenue Service.

[Note: Attached Exhibit No. 1 is a duplicate of Computation of Net Worth of Partnership printed at pages 12-13 of this printed record.]

[Endorsed]: T.C.U.S. Filed March 15, 1955.

[Title of Tax Court and Cause No. 56085.]

REPLY

The above-named petitioner, for reply to the allegations affirmatively set out by the respondent in his Answer, admits and denies as follows:

8. Referring to paragraph 8 of the Answer, petitioner alleges that she was on active duty with the United States Navy from February, 1943, to November, 1945. In March, 1945, when her return for 1944 was due, petitioner was out of the State of California on active duty with the U. S. Navy, and her return for that year was filed by her father, Nathan Sherry, pursuant to a Power of Attorney previously granted to him by petitioner. The return was prepared by accountants employed by Nathan Sherry, and on March 15, 1945, it was filed by Nathan Sherry with the Collector of Internal Revenue for the Sixth District of California. The return was not presented to petitioner for her examination of it prior to the time it was filed.

With respect to petitioner's returns for the years 1945 and 1946, those returns were also prepared by accountants employed by Nathan Sherry. The return for 1945 was filed with said Collector on March 15, 1946, and the return for 1946 was filed with said Collector on March 15, 1947.

Denies the remaining allegations of paragraph 8 of the Answer.

9. Admits that on March 15, 1946, petitioner's return for the year 1945 was filed with said Collector. Admits that on about December 14, 1950, petitioner and the Commissioner executed a waiver ex-

tending the statute of limitations to June 30, 1952, with respect to the year 1945. Admits that successive agreements were executed by petitioner and respondent further extending the statute of limitations to June 30, 1955, with respect to such year. Admits that respondent's notice of deficiency was mailed to petitioner on October 28, 1954. Denies the remaining allegations of paragraph 9 of the Answer.

10. Admits that on March 15, 1947, petitioner's return for the year 1946 was filed with said Collector. Admits that in December, 1950, petitioner and Commissioner executed a waiver extending the statute of limitations to June 30, 1952, with respect to the year 1946. Admits that successive agreements were later executed by petitioner and respondent, further extending the statute of limitations to June 30, 1955, with respect to such year. Admits that respondent's notice of deficiency was mailed to petitioner on October 28, 1954. Denies the remaining allegations of paragraph 10 of the Answer.

Denies generally and specifically each and every allegation contained in the Answer, not hereinbefore specifically admitted, qualified or denied.

Wherefore, it is prayed that the affirmative relief requested by the respondent in his Answer be denied.

/s/ CHARLES H. CARR,
/s/ WILLIAM K. RASMUSSEN,
/s/ NORMAN GOODMAN,
Counsel for Petitioner

[Endorsed]: T.C.U.S. Filed May 2, 1955.

[Title of Tax Court and Cause No. 56086.]

PETITION

The above-named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency dated October 28, 1954, and as a basis of their proceeding allege as follows:

1. Petitioner Newton Ivan Sherry is an individual with residence at 1063 - 10th Street, Hermosa Beach, California. Petitioner Lois Sherry is an individual with residence at 13408 South Vermont Avenue, Gardena, California. The returns for the years here involved were filed with the Collector at Los Angeles, California.

2. The notice of deficiency (a copy of which is attached and marked Exhibit "A") was mailed to the petitioners on October 28, 1954.

3. The deficiency as determined by the Commissioner is in income taxes as follows:

Year	Deficiency	50% Penalty
1945	$ 5,123.17	$ 3,118.79
1946	45,760.54	22,880.27
Total	$50,883.71	$25,999.06

All of the above tax deficiencies and penalties are in controversy.

4. The determination of tax set forth in said notice of deficiency is based upon the following errors:

(a) The Commissioner has erroneously deter-

mined said deficiencies and penalties because the statute of limitations under Section 275 of the Internal Revenue Code of 1939 has run on all of the above years;

(b) The Commissioner has erroneously determined that an alleged partnership called Sherry Enterprises existed and that petitioner Newton Ivan Sherry was a partner therein;

(c) The Commissioner has erroneously determined that the increase in net worth of said alleged partnership was the result of income received by such partnership;

(d) The Commissioner has erroneously used the "net worth" method to determine said deficiencies;

(e) The Commissioner has erroneously determined that petitioners received income from said alleged partnership during said years; and

(f) The Commissioner has erroneously added fraud penalties to said deficiencies. There was no intent to evade payment of income taxes.

5. The facts upon which the petitioners rely as the basis of this proceeding are as follows:

(a) Petitioners' income tax return for 1945 was filed with said Collector on or before March 15, 1946, and their return for 1946 was filed with said Collector on or before March 15, 1947. The statute of limitations (section 275 of the Internal Revenue Code of 1939) has run, therefore, on both of said years.

(b) Petitioner Newton Ivan Sherry was not a partner in any partnership known as Sherry Enterprises because there was, in fact, no such partner-

ship. But even if this Court should determine that such partnership did exist, said petitioner was not a partner therein. Petitioner Newton Ivan Sherry was on active duty with the United States Marines from 1940 to May, 1945, which included duty at Guadalcanal and vicinity from about April, 1943, to December, 1944. And from May, 1945, to July, 1946, he attended California Polytechnic College at San Luis Obispo, California. Said petitioner did not participate in any transactions or businesses involving the alleged Sherry Enterprises during any of the above taxable years. He also did not receive any money or property from the alleged partnership during said years, either as the income of such partnership or otherwise.

(c) If it should be determined that such alleged partnership did exist, petitioners allege that the partnership kept adequate books and records during said years which clearly reflect its income. Hence the Commissioner erroneously reconstructed the income of the alleged partnership by using the "net worth" method.

(d) Further, that in the event this Court determines that such alleged partnership did exist during said years and that petitioner Newton Ivan Sherry was a partner therein, petitioners allege that the increase in net worth of such partnership over and above the income reported by the partnership in its tax returns was the result of capital contributions by Nathan Sherry, the deceased father of petitioner Newton Ivan Sherry, and not as the result of income earned or received by the partner-

ship. During said years Nathan Sherry made the following capital contributions to the alleged partnership:

	Fiscal Years Ending	
	6-30-45	6-30-46
Cash	$ 4,348.00	$ 42,000.00
Bonds	5,000.00	40,000.00
Interest in partnerships	4,572.50	62,211.50
Cashier's checks	.....	60,000.00
Real Estate	17,500.00	3,000.00
Notes and Accounts Receivable	.....	5,000.00
Furniture and Fixtures	.....	2,120.00
Other	.....	30,000.00
Total	$ 31,420.50	$244,331.50

Also, the Commissioner has erroneously included as an accounts receivable of the alleged partnership on June 30, 1946, the amount of $30,000.00 as an accounts receivable due from Edward J. Margett. Edward J. Margett did not owe the alleged partnership the sum of $30,000.00 or any other amount on June 30, 1946.

Wherefore, petitioners pray that this Court may hear the proceedings and determine that there is no deficiency due from the petitioners for the years 1945 and 1946.

/s/ CHARLES H. CARR,
/s/ WILLIAM K. RASMUSSEN,
Counsel for Petitioners

Duly Verified.

EXHIBIT "A"

1250 Subway Terminal Building, 417 South Hill Street, Los Angeles 13, California

Ap:LA:AA-PAK
90D Oct. 28, 1954

Mr. Newton Ivan Sherry and Mrs. Lois Sherry, Husband and Wife,
1063 10th Street, Hermosa Beach, California

Dear Mr. and Mrs. Sherry:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1945 and December 31, 1946 discloses deficiencies in tax aggregating $50,883.71, and penalties aggregating $25,999.06, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiencies mentioned.

Within 90 days from the date of the mailing of this letter you may file a petition with The Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday, or legal holiday in the District of Columbia in which event that day is not counted as the 90th day. Otherwise Saturdays, Sundays, and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute, in duplicate, the enclosed

Exhibit "A"—(Continued)

form and forward it to the Assistant Regional Commissioner, Appellate, 1250 Subway Terminal Building, 417 South Hill Street, Los Angeles 13, California. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment, whichever is earliest.

Very truly yours,

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue
/s/ By W. T. TIGNOR,
Associate Chief, Appellate Division

Enclosures: Statement, Form 1276, Agreement Form.

PAKar:vmc

Statement

Ap:LA:AA:PAK
90D

Mr. Newton Ivan Sherry and Mrs. Lois Sherry, Husband and Wife, 1063 - 10th Street, Hermosa Beach, California.

Tax Liability for the Taxable Years Ended December 31, 1945 and December 31, 1946

Year		Deficiency	50% Penalty
1945	Income Tax	$ 5,123.17	$ 3,118.79
1946	Income Tax	45,760.54	22,880.27
	Total	$50,883.71	$25,999.06

In making this determination of your income tax and penalty liability careful consideration has been given to the report of ex-

Exhibit "A"—(Continued)

amination dated November 24, 1952, to your protest dated February 25, 1953, and to the statements made at hearings held on January 27, 1954 and July 16, 1954.

The 50 percent penalty has been asserted for each of the taxable years 1945 and 1946 under the provisions of section 293(d) of the Internal Revenue Code of 1939.

The deficiency for 1945 is assessable under the provisions of sections 275(c) and 276 of the Internal Revenue Code of 1939.

It has been determined that your share of the distributable income from Sherry Enterprises partnership is $29,889.98 for 1945 and $82,742.97 for 1946. Inasmuch as you reported $21,-841.88 in 1945 and $14,792.91 in 1946, your taxable income has been increased by the differences of $8,048.10 and $67,950.06, respectively, computed as follows:

COMPUTATION OF NET WORTH OF PARTNERSHIP

Assets:	Jun. 30, 1944	Jun. 30, 1945	Jun. 30, 1946
Cash	$ 10,322.24	($ 363.71)	$ 28,176.59
Stocks	.....	.....	.....
Bonds	50,000.00	50,000.00	50,000.00
Interest in partnerships	90,712.18	133,424.34	348,326.34
Cashier's checks	.....	2,000.00	60,000.00
Real estate	.....	118,020.42	94,619.50
Notes and accounts receivable	50,000.00	30,000.00	42,400.00
Furniture and Fixtures	.....	.....	6,743.55
Total Assets	$201,034.42	$333,081.05	$630,265.98
Liabilities:			
Accounts payable	$ 403.34	$	$ 15,000.00
Notes payable	45,000.00	40,000.00	.....
Trust deed payable	.....	21,400.00	17,500.00
Total Liabilities	$ 45,403.34	$ 61,400.00	$ 32,500.00
Net Worth	$155,631.08	$271,681.05	$597,765.98

	1945	1946
Net worth at end of year	$271,681.05	$597,765.98
Net worth at beginning of year	155,631.08	271,681.05
Increase in net worth	$116,049.97	$326,084.93

Exhibit "A"—(Continued)

	1945	1946
Additions:		
Personal expenses	6,883.00	12,127.62
Federal income tax payments	23,324.89	22,397.86
State income tax payments	573.70	.....
Payment to stock brokers	900.00	1,915.00
Purchase of personal items	.....	6,911.01
Total	$147,731.56	$369,436.42
Reductions:		
Proceeds of sale of stock	2,498.50	.....
Capital contributions	12,040.00	5,000.00
Check from brokers	10,614.31	.....
Balance	$122,578.75	$364,436.42
Add: Income adjustments:		
Ordinary income of partnership	.....	1,170.00
Short-term capital gain	(5,000.00)	(277.00)
Long-term capital gain—taxable portion	(3,989.17)	(17,178.78)
Long-term capital gain—non-taxable portion	(3,989.17)	(17,178.78)
Ordinary net income corrected	$109,600.41	$330,971.86
Ordinary net income per return	77,407.99	59,171.64
Understatement of net income	$ 32,192.42	$271,800.22
Your distributive share of amount of understatement	$ 8,048.10	$ 67,950.06

A copy of the letter and a copy of this statement have been mailed to your representative, 417 South Hill Street, Los Angeles 13, California, in accordance with the authority contained in the power of attorney executed by you.

ADJUSTMENTS TO NET INCOME

Taxable Year Ended December 31, 1945

Net income as disclosed by return	$ 22,085.98
Additional income:	
(a) Income from partnerships	10,537.97
Total	$ 32,623.95

Exhibit "A"—(Continued)

Reduction:	
(b) Long-term capital gain	742.15
Net income adjusted	$ 31,881.80

EXPLANATION OF ADJUSTMENTS

(a) Income from partnerships is increased by $10,537.97 consisting of the following:

(1) Income from Sherry Enterprises	$ 8,048.10
(2) Income from other partnerships	2,489.87
Total	$10,537.97

(1) This adjustment is previously explained herein.

(2) This adjustment was previously made to net income and agreed to by you.

(b) This adjustment was previously made to net income and agreed to by you.

COMPUTATION OF ALTERNATIVE TAX

Taxable Year Ended December 31, 1945

Net income adjusted		$ 31,881.80
Less: Excess of net long-term capital gain over net short-term capital loss		255.14
Ordinary income		$ 31,626.66
Less: Surtax exemptions		1,000.00
Surtax net income		$ 30,626.66
Ordinary net income	$ 31,626.66	
Less: Normal-tax exemptions	1,000.00	
Balance subject to normal tax	$ 30,626.66	
Normal tax at 3% of $30,626.66		$ 918.80
Surtax on $30,626.66		13,608.53
Partial tax		$ 14,527.33
Plus: 50% of $255.14		127.57
Alternative tax		$ 14,654.90

Exhibit "A"—(Continued)

COMPUTATION OF TAX

Taxable Year Ended December 31, 1945

Net income adjusted		$ 31,881.80
Less: Surtax exemptions		1,000.00
Balance subject to surtax		$ 30,881.80
Net income adjusted	$ 31,881.80	
Less: Normal tax exemptions	1,000.00	
Net income subject to normal tax	$30,881.80	
Normal tax at 3% of $30,881.80	926.45	
Surtax on $30,881.80	13,766.72	
Total normal tax and surtax	$ 14,693.17	
Alternative tax	$ 14,654.90	
Correct income tax liability		$ 14,654.90
Income tax liability shown on return, account No. 3040691	$ 8,417.31	
Additional, Oct. 1, 1948, No. 10-510048	1,114.42	9,531.73
Deficiency of income tax		$ 5,123.17
50% penalty:		
Correct income tax liability	$ 14,654.90	
Liability shown by return	8,417.31	
Excess	$ 6,237.59	
50% penalty (50% of $6,237.59)		$ 3,118.79

ADJUSTMENT TO NET INCOME

Taxable Year Ended December 31, 1946

Net income as disclosed by return	$ 20,606.85
Additional income:	
(a) Income from partnership	67,950.06
Net income adjusted	$ 88,556.91

EXPLANATION OF ADJUSTMENT

(a) This adjustment is previously explained herein.

Exhibit "A"—(Continued)

COMPUTATION OF ALTERNATIVE TAX

Taxable Year Ended December 31, 1946

Net income adjusted		$ 88,556.91
Less: Excess of net long-term capital gain over net short-term capital loss		4,294.70
Ordinary net income		$ 84,262.21
Less: Exemptions		1,000.00
Balance, subject to surtax and normal tax		$ 83,262.21
Tentative surtax	$ 50,462.39	
Tentative normal tax at 3%	2,497.86	
Total tentative tax	$ 52,960.25	
Less 5%	2,648.01	
Partial tax		$ 50,312.24
Plus: 50 percent of $4,294.70		2,147.35
Alternative tax		$ 52,459.59

COMPUTATION OF TAX

Taxable Year Ended December 31, 1946

Net income adjusted		$ 88,556.91
Less: Exemptions		1,000.00
Balance, subject to surtax and normal tax		$ 87,556.91
Tentative surtax	$ 53,941.09	
Tentative normal tax at 3%	2,626.71	
Total tentative tax	$ 56,567.80	
Less 5%	2,828.39	
Total normal tax and surtax		$ 53,739.41
Alternative tax		$ 52,459.59
Correct income tax liability		$ 52,459.59
Income tax liability shown on return, account No. 3036201		6,699.05
Deficiency of income tax		$ 45,760.54
50% penalty		$ 22,880.27

[Endorsed]: T.C.U.S. Filed January 24, 1955.

[Title of Tax Court and Cause No. 56086.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, R. P. Hertzog, Acting Chief Counsel, Internal Revenue Service, for answer to the petition of the above-named taxpayers, admits, denies and alleges as follows:

1. Denies that petitioner Lois Sherry resides at 13408 South Vermont Avenue, Gardena, California; admits the remaining allegations contained in paragraph 1 of the petition.

2, 3. Admits the allegations contained in paragraphs 2 and 3 of the petition.

4. Denies the allegations of error contained in paragraph 4 of the petition, and all subparagraphs thereof.

5 (a) Admits that petitioners' income tax return for 1945 was filed with said Collector on March 15, 1946, and their return for 1946 was filed with said Collector on March 15, 1947; denies the remaining allegations contained in subparagraph (a) of paragraph 5 of the petition.

(b), (c), (d) Denies the allegations contained in subparagraphs (b), (c) and (d) of paragraph 5 of the petition.

6. Denies generally and specifically each and every allegation contained in the petition, not hereinbefore specifically admitted, qualified or denied.

Further answering the petition, the respondent alleges that:

7. The petitioners are liable for the fifty percent fraud penalties proposed under Section 293(b) of the Internal Revenue Code of 1939 for the taxable years 1945 and 1946, in the respective amounts of $3,118.79 and $22,880.27 as determined by the Commissioner and set forth in his notice of deficiency. In support of the Commissioner's determination of such fraud penalties, the respondent alleges and relies upon the following facts:

(a) That petitioners caused to be prepared and filed with the Collector of Internal Revenue for the Sixth District of California joint income tax returns for the taxable years 1945 and 1946 and represented that each such return was a true and correct return.

(b) In truth and in fact, each of the said returns filed by the petitioners for the taxable years 1945 and 1946 was false and fraudulent in that they understated the true and correct amounts of net income and resultant tax liability thereon for each of such taxable years. The extent of the false and fraudulent understatement of net income and income tax liability for each of such years is as follows:

Year	Net Income Reported	Tax Liability Reported	Correct Net Income	Correct Tax Liability
1945	$22,085.98	$8,417.31	$31,881.80	$14,654.90
1946	20,606.85	6,699.05	88,556.91	52,459.59

(c) At the time the aforesaid returns for the tax-

able years 1945 and 1946 were prepared and filed, the petitioners knew that such returns were false and fraudulent, and that the amount of net income reported therein and the resultant tax liability shown thereon were understated in each of the said returns. The petitioners knowingly, wilfully and fraudulently made and filed their income tax returns for the taxable years 1945 and 1946 with intent to deceive respondent and evade tax.

(d) During the taxable years in question, petitioners derived and received income from partnership operations conducted under the partnership name of Sherry Enterprises.

(e) Books and records pertaining to the income producing activities of the aforementioned partnership during the years in question were too inadequate and insufficient to enable the Commissioner, through his examining agents, to check and verify the partnership's correct net income and petitioners' share thereof for the taxable years 1945 and 1946; said records were inadequate in that they were incomplete as to some of the partnership's income producing activities and no records were kept of other partnership income producing activities. Consequently, it became necessary for the Commissioner to determine the correct amounts of taxable net income for the years involved from other sources of information. The Commissioner, through his examining and investigating agents determined the taxable income of the partnership for such years by the "Net Worth and Expenditure Method."

(f) The corrected income of the partnership and the petitioners' share thereof is determined for the taxable years 1945 and 1946 by reference to the increase in net worth of the partnership during such years, as shown in Exhibit 1 attached to this answer and incorporated herein by reference.

(g) The understatement of petitioners' income and income tax liability for each of the taxable years 1945 and 1946 was due to fraud with intent to evade tax.

(h) Petitioners having filed a false and fraudulent return with intent to evade tax for the taxable year 1945 neither the assessment nor collection of the proposed deficiency is barred by any statute of limitations under the provisions of Section 276(a) of the Internal Revenue Code of 1939.

8. Further answering the petition, for an alternative defense, respondent alleges that the five-year period of limitation is applicable under Section 275(c) of the Internal Revenue Code of 1939 for assessment and collection of the deficiency determined by the Commissioner for the taxable year 1945 as set forth in the notice of deficiency. In support of such determination, respondent alleges as follows:

(a) On March 15, 1946 petitioners filed their return for the year 1945 with the Collector of Internal Revenue for the Sixth District of California.

(b) Petitioners improperly omitted from gross income reported for the year 1945 an amount properly includible therein which is in excess of 25

per centum of the amount of gross income stated in the return.

(c) On December 14, 1950, and within five years after filing petitioners' income tax return for 1945, the petitioners and the Commissioner duly executed a waiver consenting to the assessment and collection of any deficiency which might be determined for the year 1945 predicated upon the Commissioner's proper inclusion in petitioners' gross income of an amount in excess of 25 percent of the gross income stated in their return and the application of the five-year statutory period of limitation as provided under Section 275(c) of the Internal Revenue Code. Successive agreements were later timely executed by petitioners and respondent, further extending the statute of limitations until June 30, 1955 with respect to such taxable year. Respondent's notice of deficiency mailed to petitioners on October 28, 1954 was timely mailed under the provisions of Section 275(c) and 276(b) of the Internal Revenue Code of 1939.

9. Further answering the petition, respondent alleges as follows:

(a) On March 15, 1947 petitioners filed their return for the year 1946 with the Collector of Internal Revenue for the Sixth District of California. On March 6, 1950, and before the expiration of the three-year statute of limitations with respect to the year 1946, the petitioners and the Commissioner duly executed a waiver extending the statute of limitations. Successive agreements were later timely

executed by petitioners and respondent, further extending the statute of limitations until June 30, 1955 with respect to such taxable year. Respondent's notice of deficiency mailed to petitioners on October 28, 1954 was timely mailed under the provisions of Section 276(b) of the Internal Revenue Code of 1939.

Wherefore, it is prayed:

1. That the relief sought in the petition be denied.

2. That the deficiencies in income taxes for the taxable years 1945 and 1946, as set forth in the notice of deficiency, be in all respects approved.

3. That the deficiencies in fraud penalties for the taxable years 1945 and 1946, as set forth in the notice of deficiency, be in all respects approved.

4. That this Court find and hold that the assessment and collection of the proposed deficiency for the taxable year 1945 is not barred by any statute of limitations under the provisions of Section 276(a) of the Internal Revenue Code for 1939.

5. In the alternative, that this Court enter its decision that petitioners improperly omitted from gross income reported for the year 1945 an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in such return; that for the year 1945 the five-year period of limitation for assessment and collection of the income tax deficiency for such year attaches

pursuant to Section 275(c) of the Internal Revenue Code of 1939; that the Commissioner's notice of deficiency mailed to petitioners on October 28, 1954 was timely under the provisions of Sections 275(c) and 276(b) of the Internal Revenue Code of 1939; and that the assessment and collection of the deficiencies for the years 1945 and 1946 is not barred.

/s/ R. P. HERTZOG, ECC.
Acting Chief Counsel, Internal Revenue Service.

Of Counsel: Melvin L. Sears, Regional Counsel, E. C. Crouter, Assistant Regional Counsel, R. E. Maiden, Jr., Special Assistant to the Regional Counsel, Mark Townsend, Attorney, Internal Revenue Service.

[Note: Exhibit 1 attached is a duplicate of Computation of Net Worth of Partnership printed in full at pages 32-33 of this printed record.]

[Endorsed]: T.C.U.S. Filed March 15, 1955.

[Title of Tax Court and Cause No. 56086.]

REPLY

The above-named petitioners, for reply to the allegations affirmatively set out by the respondent in his Answer, admit and deny as follows:

7. Referring to paragraph 7 of the Answer, petitioners allege that for the years 1945 and 1946 their joint returns were filed with the Collector of

Internal Revenue for the Sixth District of California. Deny the remaining allegations of paragraph 7 of the Answer.

8. Referring to paragraph 8 of the Answer, petitioners allege that on March 15, 1946, their return for the year 1945 was filed with said Collector. Admit that in December, 1950, petitioners and the Commissioner executed a waiver extending the statute of limitations to June 30, 1952, with respect to the year 1945. Admit that successive agreements were executed by petitioners and respondent further extending the statute of limitations to June 30, 1955, with respect to such year. Admit that respondent's notice of deficiency was mailed to petitioners on October 28, 1954. Deny the remaining allegations of paragraph 8 of the Answer.

9. Referring to paragraph 9 of the Answer, petitioners allege that on March 15, 1947, their return for the year 1946 was filed with said Collector. Admit that in December, 1950, petitioners and Commissioner executed a waiver extending the statute of limitations to June 30, 1952, with respect to the year 1946. Admit that successive agreements were later executed by petitioners and respondent further extending the statute of limitations to June 30, 1955, with respect to such year. Admit that respondent's notice of deficiency was mailed to petitioners on October 28, 1954. Deny the remaining allegations of paragraph 9 of the Answer.

Deny generally and specifically each and every

allegation contained in the Answer, not hereinbefore specifically admitted, qualified or denied.

Wherefore, it is prayed that the affirmative relief requested by the respondent in his Answer be denied.

/s/ CHARLES H. CARR,
/s/ WILLIAM K. RASMUSSEN,
/s/ NORMAN GOODMAN,
Counsel for Petitioner

[Endorsed]: T.C.U.S. Filed May 2, 1955.

[Title of Tax Court and Cause Nos. 56085-56086.]

MINUTES OF PROCEEDINGS

Date: April 15, 1957. Place: Los Angeles, Calif. Docket Nos. 56085, 56086.

Proceeding: Margaret Lillian Ferguson, et al.

Judge: Arnold Raum, Division No. 11.

Counsel: For Petitioner, Charles H. Carr, Esq., 403 Subway Terminal Bldg., 417 S. Hill St., Los Angeles 13. For Respondent, Mark Townsend, Esq.

Stenographic Reporter: Miriam Polk. Transcript ordered: Yes.

Hearing of trial commenced at 11:10 a.m. Closed at 4:40 p.m. On the merits: Yes.

On motion: Joint oral motion to consolidate cases for trial—Granted.

Action: Submitted.

Filed at hearing: Stipulation of facts.

Petitioner's brief: May 31, 1957.

Respondent's brief: July 1, 1957.

Pet. reply: July 22, 1957.

Witnesses: For Petitioner, Herndon Hughes, Newton Sherry, Margaret Ferguson, Paul Kalmanovitz, James F. Murray. For Respondent, William B. Burns.

Exhibits: Petitioner's: None. Respondent's: Resp. exhibits A thru J—attached to stipulation of facts and described therein. K—Waiver and Rev. Agent's Report. L—Waiver and Rev. Agent's Report. M—Sworn statement of Margaret Ferguson.

/s/ GEORGE J. BAIRD,
Deputy Clerk

The Tax Court of the United States

Docket No. 56085

Margaret Lillian Ferguson, Petitioner, vs. Commismissioner of Internal Revenue, Respondent.

Docket No. 56086

Newton Ivan Sherry, Lois Sherry, Petitioners, vs. Commissioner of Internal Revenue, Respondent.

Docket No. 56087

Newton Ivan Sherry, Petitioner, vs. Commissioner of Internal Revenue, Respondent.

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto by their respective counsel of record that the following facts shall be taken as

true without prejudice to the right of either party to submit material and competent evidence of any other facts not inconsistent herewith:

1. Newton Ivan Sherry and Margaret Lillian Ferguson (nee Sherry) are the son and daughter of Nathan Sherry, deceased. Lucille Lawler Sherry is their stepmother. Lois Sherry is the wife of Newton Ivan Sherry.

2. The only issue with respect to income is whether or not these petitioners are taxable on a distributable share of the income of Sherry Enterprises, since petitioners Margaret Lillian Ferguson and Newton Ivan Sherry contend that they were not partners in Sherry Enterprises. Petitioners do not contest respondent's determination that the net worth statements set forth in the notices of deficiency reflect the income of Sherry Enterprises for the fiscal years 1945 and 1946, because they state they have no knowledge or information regarding the same.

3. The respondent concedes that the deficiencies determined herein against the petitioners are not due to fraud with intent to evade tax and that the provisions of section 293(b) IRC of 1939 are not applicable.

4. The statute of limitations has expired for the year 1944 as to the petitioners. Due to waivers duly signed by petitioners and the respondent after the expiration of the three-year statute of limitations, the year 1945 is open only in the event the provisions of section 275(c) IRC of 1939 are held ap-

plicable thereto. Due to waivers duly signed by petitioners and the respondent the three-year statute of limitations has not expired with respect to the year 1946.

5. Attached hereto and marked respondent's exhibits A and B are true copies of petitioner Margaret Lillian Ferguson's returns filed for the years 1945 and 1946, respectively, which returns bear the signatures of petitioner Margaret Lillian Ferguson.

6. Attached hereto and marked respondent's exhibits C and D are true copies of the joint returns of petitioners Newton Ivan Sherry and Lois Sherry filed for the years 1945 and 1946, respectively, which returns bear the signatures of said petitioners.

7. Attached hereto and marked respondent's exhibits E and F are true copies of Forms 1065 of the Sherry Enterprises filed for the years ending June 30, 1945 and June 30, 1946, respectively.

8. Attached hereto and marked respondent's exhibits G and H are true copies of Articles of Co-Partnership and amendment thereto, respectively, signed by petitioners Newton Ivan Sherry and Margaret Lillian Ferguson (nee Sherry), their father, Nathan Sherry, and their stepmother, Lucille Lawler Sherry. Said Articles of Co-Partnership and amendment thereto were prepared by Ned Williams, an attorney at law, who is now deceased.

9. Attached hereto and marked respondent's exhibits I and J are gift tax returns of Nathan

Sherry and Lucille Lawler Sherry, respectively, for the year 1943, which exhibits include donee information returns of Newton Ivan Sherry and Margaret Lillian Ferguson (nee Sherry).

/s/ WM. K. RASMUSSEN,
Counsel for Petitioners
/s/ NELSON P. ROSE, REM.
Chief Counsel, Internal Revenue Service, Counsel for Respondent

[Endorsed]: T.C.U.S. Filed April 15, 1957.

T. C. Memo. 1958-32

Tax Court of the United States

Margaret Lillian Ferguson, Petitioner, vs. Commissioner of Internal Revenue, Respondent.
Newton Ivan Sherry, Lois Sherry, Petitioners, vs. Commissioner of Internal Revenue, Respondent.

Docket Nos. 56085, 56086

Filed February 26, 1958

Charles H. Carr, Esq., for the petitioners.
Mark Townsend, Esq., for the respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

Respondent determined the following deficiencies:

Margaret Lillian Ferguson, Docket No. 56085:
Year 1944—Income Tax, $5,817.27. Additions for Fraud, $2,908.63.

Year 1945—Income Tax, $5,124.55. Additions for Fraud, $3,117.15.

Year 1946—Income Tax, $45,333.52. Additions for Fraud, $22,666.76.

Newton Ivan Sherry and Lois Sherry, Docket No. 56086:

Year 1945—Income Tax $5,123.17. Additions for Fraud, $3,118.79.

Year 1946—Income Tax, $45,760.54. Additions for Fraud, $22,880.27.

It was stipulated that no fraud is applicable to any of the years involved herein, and that the statute of limitations has expired for the year 1944.

At issue is whether Newton Ivan Sherry and Margaret Lillian Ferguson were members of a partnership during the years 1945 and 1946.

Findings of Fact

Some of the facts were stipulated and are hereby incorporated as part of these findings.

Petitioners Newton Ivan Sherry (hereinafter referred to as "Newton") and Margaret Lillian Ferguson (hereinafter referred to as "Margaret") are the children of Nathan Sherry (hereinafter referred to as "Nathan"). Nathan's first wife, the mother of Newton and Margaret, died in 1937. In 1938 Nathan married Lucille Lawler Sherry (hereinafter referred to as "Lucille"). Nathan died in 1954. Petitioner Lois Sherry is the wife of Newton, and, aside from the fact that she filed joint returns with Newton, has no connection with the issue here involved.

Petitioners' returns for the calendar years 1945 and 1946 were filed with the collector of internal revenue for the sixth district of California.

Nathan, after discussions with his lawyer and his accountants, had his lawyer draft a partnership agreement dated October 1, 1943, which stated in part:

Whereas, First Parties [Nathan and Lucille] were married on the first day of April, 1938 and ever since said date have been and now are husband and wife; and

Whereas, since said marriage First Parties have acquired and now own and hold the hereinafter described properties as community property; and

Whereas, First Parties acquired all of said properties by and through their joint and several personal services actually rendered since the date of said marriage; and

That said properties are described as follows:

50% interest of S & P Company valued at $30,000.00;

25% interest of Hollywood Recreation Company valued at $25,000.00;

100% interest of Hollyway Cafe valued at $5,000.00;

50% interest of Monticello Cafe valued at $4,500.00;

33⅓% interest of Pago Cafe valued at $3,000.00;

12½% interest of Swing Club valued at $1,500.00; and

Whereas, Second Parties are the children of Nathan Sherry by a former marriage, and there

are no children the issue of said marriage of First Parties, and

Whereas, First Parties desire to give and transfer to Second Parties one-half of their interest in the afore-described properties for the purpose of creating a partnership between and including all and every of parties hereto,

Now, Therefore, Be It Known by These Presents:

That the parties hereto will become and remain partners for a term of one year if each and all of them shall so long live, and for and during such additional time as each and all shall so desire;
* * * * *

The S & P Company (hereinafter referred to as "S & P") owned and operated bars and restaurants. Paul Kalmanovitz owned the remaining 50 per cent interest in S & P.

The partnership agreement, along with a letter requesting their signatures, was mailed to Newton, who was then on Guadalcanal as a member of the United States Marines, and to Margaret who was then stationed in Ohio as a member of the United States Navy. They, in turn, signed the agreement and mailed it back to their father who was in Los Angeles. At the time they signed the agreement Newton was 23 and Margaret was 20.

Nathan and Lucille filed gift tax returns dated March 15, 1944, for the year 1943 on which they each reported gifts of one-half the property transferred to the new firm. Margaret signed donee returns dated March 15, 1944, in connection there-

with. Nathan signed donee returns as attorney in fact for Newton.

The parties to the original agreement signed an amendment thereto dated July 1, 1944. This amendment stated that the firm's losses were to be borne in equal shares by the parties to the agreement. The amendment indicates that the firm was named Sherry Enterprises (hereinafter referred to as "Enterprises").

Newton was on active duty with the Marines from January 1940 until May 1945. He returned to the United States in March 1945, and was in a hospital in Philadelphia, Pennsylvania, from then until May 1945. Margaret was on active duty with the Navy from February 1943 until November 1945.

Throughout the period relevant to this proceeding Nathan possessed a power of attorney to act in behalf of Newton and Margaret.

Partnership returns for Enterprises for fiscal years beginning July 1, 1944, and ending June 30, 1945, and beginning July 1, 1945, and ending June 30, 1946, dated September 13, 1945, and September 3, 1946, respectively, were signed by Nathan. Petitioners did not examine, sign or have anything to do with the preparation of these returns. Their preparation and filing were carried out under Nathan's direction.

At Nathan's direction accountants prepared the individual returns of Newton and Margaret for the calendar years 1945 and 1946. These returns disclosed that Newton and Margaret each had $21,-

599.28 of income from Enterprises in 1945 and $19,156.85 in 1946. Petitioners signed their respective 1945 returns on March 13, 1946. The returns for 1946, signed by petitioners, were received in the office of the collector of internal revenue on March 15, 1947. Nathan saw to the preparation and filing of these returns and also arranged for the payment of the tax shown to be owing on the returns.

Newton enrolled in college for the fall semester of 1945, but dropped out before completion of the semester in order to work for S & P. This was done in response to directions from Nathan. Newton was employed by S & P as manager of a drive-in and bar known as the Bayview Club. His salary was $110 per week. This job ended sometime in 1946. At no time during this employment did Newton have anything to do with the keeping of the books and records of the Bayview Club.

In 1946 Newton purchased a home for $8,599. The money for this purchase was given to him by his father. The house was sold later in that same year and the money was returned to Nathan. Newton always considered that the house belonged to Enterprises.

Margaret attended college during the spring semester of 1946. In the fall of that year she worked as an office girl in a perfume business named Sherry Dunn. Margaret believed that this business was owned by Enterprises.

At Nathan's request Margaret sometimes made deposits and withdrawals for him at various banks.

At some of these banks the accounts were in the joint names of Margaret and Nathan. During the period in which Margaret lived in her father's home she drew on these accounts to meet their household expenses. Margaret was married in March 1947 and ceased to live in her father's home.

At the time of their mother's death and in the years following, Newton and Margaret were under the impression that their mother had left them $20,000 in the care of their father. It was their belief that Nathan used this money in his business, and that it was part of the capital of Enterprises.

Sometime after their discharge from the Armed Forces Newton and Margaret each received approximately $500 as a result of the death of a grandparent. They turned this money over to Nathan to be used in Enterprises.

In 1945 real property valued at approximately $52,500 was placed in Margaret's name. In 1946 real property valued at approximately $2,500 was also placed in her name. All of this property was placed in her name at Nathan's direction. Margaret did not consider herself the owner of this property. She thought it belonged to Enterprises.

In 1947 Nathan transferred stock in the Marguery Corporation, which operates Lucy's restaurant, to Margaret. Nathan had purchased this business with funds from Enterprises. Margaret, at the time of the transfer from her father, considered herself the owner of the transferred shares. For a time Margaret was president of the corporation;

at the time of the trial she managed the restaurant and owned 20 per cent of the corporation's outstanding stock.

Margaret is the record owner of a "fourplex" apartment house valued at approximately $14,000. Her rights in this property were transferred to her by her father. It was subject to an existing attorney's lien, and there is now an outstanding "assignment" of her rights in this property.

Margaret is the owner of a "triplex" apartment house valued at approximately $35,000. This house belonged to Enterprises prior to its transfer to Margaret in 1950. Since the transfer of the "triplex" Margaret has made all the mortgage payments thereon.

Newton and his wife signed a "Waiver of Restrictions on the Assessment and Collection of Deficiency in Tax" (Form 870) dated July 19, 1948 for the year 1945 for the amount of $1,114.42. The address under their signatures is 5444 Melrose Avenue, Los Angeles. Lucy's restaurant is located at that address. In a letter dated September 9, 1948, mailed to the Melrose Avenue address, respondent indicated that the deficiency was caused by an increase in Newton's distributive share of Enterprises' income.

On November 2, 1949, in the course of the Internal Revenue Service's investigation of Nathan's income, Newton testified under oath that he was then a partner in Enterprises.

Margaret signed a "Waiver of Restrictions on

Assessment and Collection of Deficiency in Tax" dated July 1948 for the year 1945 for the amount of $1,109.75. The address under Margaret's signature was 5444 Melrose Avenue, Los Angeles. In a letter dated September 9, 1948, mailed to the Melrose Avenue address, respondent indicated that the deficiency was caused by an increase in Margaret's distributive share of Enterprises' income.

On May 15, 1950, in the course of the Internal Revenue Service's investigation of Nathan's income, Margaret testified under oath that she was then a partner in Enterprises.

In 1947 S & P was dissolved. Neither Newton nor Margaret had any connection with the negotiations leading to a division of that company's property.

One of the former S & P properties not taken by Paul Kalmanovitz upon dissolution of that company was the Clover Club and its underlying real property. This property was placed in a trust the beneficiaries of which were Newton and Margaret. The trustee of this trust was an accountant employed by Nathan. The Clover Club was later destroyed by fire. Subsequently this property was sold. Nathan received the proceeds of the sale. The trustee did nothing to protect the interests of the beneficiaries. Nathan was in control of Enterprises; however, at various times he, his wife, Newton and Margaret held informal meetings at which Enterprises' business was discussed.

The earliest that Paul Kalmanovitz heard of the existence of Enterprises was 1947.

Newton and Margaret never asked to examine, or examined any of the books or records of Enterprises or of S & P. Nor did they ever request an accounting in connection with either of these firms.

Respondent increased the income of Sherry Enterprises for the years relevant to petitioners' taxable years 1945 and 1946, and accordingly increased their distributive shares and their income taxes for those years.

Petitioners Newton and Margaret were partners in Sherry Enterprises during the years in question.

Opinion

Raum, Judge: This case presents the reverse of the usual family partnership controversy. Here, petitioners seek to disavow the existence of the partnership. The burden of proof is upon them, and we cannot find on this record that it has been carried.

The picture is far from clear on the evidence before us. It does appear that petitioners'[1] father had a number of business interests involving restaurants, bars, and taverns. These enterprises were operated by various organizations, the principal one being the S & P Company, a partnership in which the father had a 50 per cent interest. In October 1943 a document entitled "Articles of Co-Partnership" was executed by petitioners, their father and stepmother. It identified various business interests, recited that they were held as community property

[1] For convenience, the word "petitioners" is used to refer to Margaret and Newton.

by the father and stepmother who wished to give one-half of their interest to petitioners for the purpose of creating a partnership between all of the parties, and undertook to establish an equal partnership among them. A further agreement, dated July 1, 1944, amended the foregoing in certain particulars; it referred to the partnership as "Sherry Enterprises", and was signed by all four parties. Sherry Enterprises was not an operating company; it merely owned the interests in the various enterprises previously held by petitioners' father.

Petitioners emphasize the fact that neither of them rendered significant services to Sherry Enterprises, but this is not surprising since it was in the nature of a holding company. Moreover, each signed the original partnership agreement as well as the amendment thereto. Gift tax returns were filed. Each petitioner filed income tax returns reporting a share of distributable income of Sherry Enterprises. Each was questioned under oath by Government agents (Newton in 1949 and Margaret in 1950) during the course of an investigation of their father's affairs, and each swore that he or she was a partner. Also, in 1948, Newton signed a document authorizing the assessment and collection of $1,114.42 additional income taxes for 1945 based upon his distributive share of revised earnings of Sherry Enterprises, and Margaret signed a similar document authorizing the assessment and collection of $1,109.75 additional income taxes for 1945 based upon her distributive share of those revised earn-

ings. We have reexamined petitioners' testimony in the light of the entire record and are not convinced that they have satisfactorily explained away the obvious conclusions to be drawn from these facts. Additionally, notwithstanding some broad denials, we are far from satisfied that neither in fact received substantial distributions from Sherry Enterprises, directly or indirectly. We cannot conclude on the record before us that petitioners were not in fact bona fide partners in Sherry Enterprises during the years in question.

It is doubtful whether, apart from the gifts, either of them contributed substantial amounts of capital to the partnership. To be sure, each at a later time did contribute $500 which had been inherited from a grandparent, and there is some suggestion that an amount of approximately $20,000, said to have been inherited from their mother, found its way into the partnership, but the evidence on this was too unsatisfactory for us to make any finding that such was in fact the case, although they believed that $20,000 had been left to them by their mother and invested in Sherry Enterprises. Perhaps, if the burden of proof were on the Government, we would hold in favor of petitioners. But the burden is not upon the Government; it is upon petitioners, and we cannot find from the evidence presented that they were not in fact partners in Sherry Enterprises during the tax years. Accordingly, we have found as a fact that they were partners during the years in controversy. Cf. Maletis vs. United States, 200 F. 2d 97 (C.A. 9), affirming 97 F. Supp. 562

(D. Ore.); Love vs. United States, 96 F. Supp. 919, 921 (C. Cls.); Higgins vs. Smith, 308 U.S. 473, 477.

Decisions will be entered under Rule 50.

Tax Court of the United States
Washington

Docket No. 56085

MARGARET LILLIAN FERGUSON,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the memorandum findings of fact and opinion filed herein February 26, 1958, directing that decision be entered under Rule 50, the parties, on May 14, 1958, filed an agreed computation for entry of decision. It is therefore

Ordered and Decided: That there are deficiencies in income tax and additions to tax as follows:

Year 1944—Income Tax, None; Additions to Tax Sec. 293(b), I.R.C. 1939: None.

Year 1945—Income Tax: $5,124.55; Additions to Tax Sec. 293(b), I.R.C. 1939: None.

Year 1946—Income Tax: $45,333.52; Additions to Tax Sec. 293(b), I.R.C. 1939: None.

[Seal] /s/ ARNOLD RAUM,
Judge

Entered May 19, 1958. Served May 21, 1958.

Tax Court of the United States
Washington

Docket No. 56086

NEWTON IVAN SHERRY, LOIS SHERRY,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the memorandum findings of fact and opinion filed herein February 26, 1958, directing that decision be entered under Rule 50, the parties, on May 14, 1958, filed an agreed computation for entry of decision. It is therefore

Ordered and Decided: That there are deficiencies in income tax in the amounts of $5,123.17 and $45,760.54 for the taxable years 1945 and 1946, respectively, and that there are no additions to tax under section 293 (b), I.R.C. 1939, for the years 1945 and 1946.

[Seal] /s/ ARNOLD RAUM,
Judge

Entered May 19, 1958. Served May 21, 1958.

[Title of Tax Court and Cause Nos. 56085-6.]

PETITION FOR REVIEW

Margaret Lillian Ferguson, Newton Ivan Sherry, and Lois Sherry, the petitioners in the above entitled matters, heretofore consolidated for purposes of trial, by Charles H. Carr, their attorney, hereby file their Petition for Review by the United States Court of Appeals for the Ninth Circuit of the decisions by the Tax Court of the United States, entered on May 19th, 1958, ... Tax Court ...., Memo. 1958-32, determining deficiencies in the petitioners' Federal income taxes for the calendar years 1945 and 1946, as follows:

Margaret Lillian Ferguson: 1945, $5,124.55; 1946, $45,333.52.

Newton Ivan Sherry and Lois Sherry: 1945, $5,-123.17; 1946, $45,760.54;

and said petitioners respectfully show:

I.

Jurisdictional Statement

The petitioners are residents of the Southern District of California and filed their respective income tax returns for the calendar years 1945 and 1946 with the Collector of Internal Revenue for the Sixth District of California, at Los Angeles, California; that, pursuant to the provisions of Section 7482(b)(1) of Title 26, U. S. Code, the venue for review of said decisions is the United States Court of Appeals for the Ninth Circuit.

II.

Nature of Controversy

Newton Ivan Sherry and Lois Sherry were, during the calendar years 1945 and 1946, husband and wife; Margaret Lillian Ferguson is the sister of Newton Ivan Sherry.

The controversy involves the proper determination of the petitioners' liability for Federal income taxes for the calendar years 1945 and 1946.

The controversy arises from the holding of the Commissioner of Internal Revenue that Newton Ivan Sherry and Margaret Lillian Ferguson were, during each of said years, co-partners with their father, Nathan Sherry (now deceased), and their stepmother, Lucille Lawler Sherry. Petitioner Lois Sherry's only connection with the issues involved is the fact that she filed joint returns with her husband, Newton Ivan Sherry. The deficiencies in income tax held by the Commissioner of Internal Revenue with respect to the years 1945 and 1946 arose entirely from the failure of the petitioners to include income from the alleged partnership in their personal income tax returns.

III.

Relief Sought

The said petitioners, being aggrieved by the Findings of Fact and Conclusions of Law contained in the Memorandum Findings of Fact and Opinion of the Court, and by its decisions pursuant thereto, desire to obtain a review thereof by the United

States Court of Appeals for the Ninth Circuit.

/s/ CHARLES H. CARR,
Counsel for Petitioners

Duly Verified.

[Endorsed]: T.C.U.S. Filed June 16, 1958.

[Title of Tax Court and Cause Nos. 56085-6.]

CERTIFICATE

I, Howard P. Locke, Clerk of the Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 30, inclusive, constitute and are all of the original papers as called for by the "Designation of Contents of Record on Review", including Respondent's Exhibits A through J, attached to Stipulation of Facts and Respondent's Exhibits K, L and M, admitted in evidence, in the cases before the Tax Court of the United States docketed at the above numbers and in which the petitioners in the Tax Court have filed a petition for review as above numbered and entitled, together with a true copy of the docket entries in said Tax Court cases as the same appear in the official docket in my office.

In testimony whereof, I hereunto set my hand and affix the seal of the Tax Court of the United States, at Washington, in the District of Columbia, this 8th day of July, 1958.

[Seal] /s/ HOWARD P. LOCKE,
Clerk, Tax Court of the United States

The Tax Court of the United States

Docket Nos. 56085, 56086 and 56087

MARGARET LILLIAN FERGUSON, et al.,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

TRANSCRIPT OF PROCEEDINGS

Court Room No. 10, Federal Building, Los Angeses, California, April 15, 1957—11:00 a.m.

(Met pursuant to notice.)

Before: Honorable Arnold Raum, Judge.

Appearances: Charles H. Carr, Esq., and William K. Rasmussen, Esq., Suite 403, 417 South Hill Street, Los Angeles 13, California, appearing on behalf of the Petitioners. Mark Townsend, appearing on behalf of the Respondent. [1*]

* * * * *

Whereupon,

HERNDON HUGHES

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: State your name, Mr. Witness, and your address.

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* Page numbers appearing at top of page of Reporter's Transcript of Record.

(Testimony of Herndon Hughes.)

The Witness: Herndon Hughes, Residence address?

The Clerk: That's all right.

The Witness: 313 Blythe Road, Pasadena.

Direct Examination

Q. (By Mr. Carr): What is your occupation, please? A. I am an accountant.

Q. And how long have you been so employed?

A. Approximately 15 years.

Q. Were you acquainted with Mr. Nathan Sherry before [7] he was deceased?

A. I was.

Q. And did you have anything to do with his drawing up a partnership agreement?

A. Yes. I was an accountant for Mr. Sherry at the time that partnership was drawn.

Q. What was Mr. Sherry's business at that time, Mr. Nathan Sherry?

A. He was a restaurant-bar owner.

Q. And I believe, if I may not lead too much —counsel, you call me if I do—that there were several restaurants involved in the partnership, were there?

A. I think there were six, yes, sir.

Q. The name of that company?

A. S & P Company was the primary partnership.

Q. Who were the partners, do you know?

A. Mr. Nathan Sherry, Mr. Paul Kalmanovitz.

(Testimony of Herndon Hughes.)

Q. Did Mr. Sherry consult with you about setting up a family partnership?

A. Yes, sir, he did.

Q. And did you do anything as a result of that?

A. Yes, sir.

Q. Tell us what you did.

A. Mr. Sherry talked to us about the possibility of a partnership, and I believe that Mr. George Williams is the name [8] of the attorney that was called in, and we had a conference in which Mr. Williams, Mr. Sherry, myself, I believe my partner, Paul Yessner, were present.

Q. May I interrupt you? Mr. Williams is dead, is he not?

A. I don't know, Mr. Carr.

Mr. Carr: Counsel, I believe you will stipulate——

Mr. Townsend: We have so stipulated.

Mr. Carr: That is right, the attorney is dead.

Q. (By Mr. Carr): As the result of that did Mr. Williams draft an agreement?

A. He did. He drafted a partnership agreement.

Q. And that——

Mr. Carr: I take it, counsel, the stipulation is that that is the agreement which is on file?

Mr. Townsend: Right.

Q. (By Mr. Carr): As a result of that, did you draft some gift tax returns?

A. Oh, yes, sir.

(Testimony of Herndon Hughes.)

Mr. Carr: May I see that just a moment, your Honor?

Q. (By Mr. Carr): Will you just find, if you can, the two gift tax returns there, please, Mr. Hughes?

Are those the ones you prepared, or copies, rather, [9] photostatic copies of the ones you prepared? A. Yes, sir.

Q. Now, did you ever at any time to your knowledge know——

The Court: Did you identify them with exhibit numbers?

The Witness: The Exhibit I and J.

Q. (By Mr. Carr): Did you ever at any time hear Mr. Sherry, Mr. Nathan Sherry, have a conversation or discuss those gift tax returns or the partnership agreement with either one of the children, Margaret or Newton? A. No, sir.

Q. Did you ever at any time have any discussion yourself with either Margaret or Newton before these returns were prepared or during the time? A. No, sir.

Q. Were you acquainted with the operation of the business? A. Yes, sir.

Q. To your knowledge, did either one of these children ever have anything to do with the business operation?

A. At the time these returns——

Q. Or after, yes.

A. I wouldn't say after, Mr. Carr, but at the time that the gift tax return was filed I am quite

(Testimony of Herndon Hughes.)

sure that neither of the children had anything to do with the partnership.

Q. They were away in service, weren't they?

A. Yes, sir.

Q. Do you remember when they returned from the service?

A. No, sir, I don't, but in my recollection, they were both in the service until some time in 1945.

Q. And during that period of time who, if you know, attended to the books of the partnership? That was known as Sherry Enterprises, is that right?

A. This partnership was known as Sherry Enterprises.

Q. That is the one in which the wife and the two children and Mr. Sherry were partners?

A. That is correct. I believe that Mr. Maurice Kahn had the records. I am not quite sure about that.

Q. Was he in your firm?

A. Yes, he was in our office, not in our firm.

Q. The books and records, the work done on them, the preparation of the partnership returns was done by whom?

A. By Mr. Kahn or myself. The returns I prepared myself.

Q. At whose request?

A. At Mr. Sherry's request.

Q. And by that you mean Mr. Nathan Sherry?

A. Yes.

Q. Now, did you ever receive a request at any

(Testimony of Herndon Hughes.)

time from either of these two children, Margaret or Newton, to prepare a tax return in connection with that partnership?

A. When was the last partnership return? [11]

Q. We are dealing with '45 and '46 here, '44, '45, and '46.

A. As I recall it, Mr. Carr, the children came out of the Service, came home from the Service in the latter part of 1945, and shortly thereafter, shortly after their return I saw both of them within the first month, I would say, after their return, I saw both of them. We had some discussions, business, and what they planned to do.

Q. I am not talking about generally now. I am talking about, did either one of these children ever specifically ask you at any time to prepare a partnership return?

A. No, no, Mr. Sherry would be the one.

Q. Mr. Nathan Sherry is the one who made the request?

A. The person who asked us to prepare the return.

Q. Will you turn to the exhibits, the returns of the two children, the individual returns? Do you find those? Give me the exhibit numbers, please, the letters.

A. Yes, I have them.

Q. Give us the letters, will you, please?

A. Margaret Lillian Sherry for the year 1945 is Exhibit A; Margaret Lillian Sherry for the year 1946 is Exhibit B; Newton Ivan and Lois Sherry

(Testimony of Herndon Hughes.)

for the year 1946 is Exhibit D, and Newton Ivan and Lois Sherry for the year 1945 is Exhibit C.

Q. Now, those returns were prepared by your concern, were they? A. Yes, sir. [12]

Q. And——

A. Wait one moment, with the exception of Exhibit D.

Q. That is the return of whom?

A. No, with the exception of Exhibit B and D.

Q. Now, they are what?

A. That is the 1946 return of both children; that would be Margaret.

Q. Now, A and C are the returns for 1946, is that correct? A. '45.

Q. I mean '45, thank you. A. Yes, sir.

Q. Now, those were prepared by your——

A. Yes, sir, myself.

Q. Your firm? A. I prepared them.

Q. And where did you send them to, to have the children sign them, and at whose request?

A. I would have to call on my recollection. My recollection is, I gave the returns to Mr. Nathan Sherry. That would be the returns for himself and his wife, Sherry Enterprises, and Margaret and Newton's returns, and Mr. Sherry had them delivered back to me. That is my recollection. To tell you specifically what happened, I can't, Mr. Carr.

Q. All I am asking is your best recollection. Then, as [13] I understand it, at no time did either Margaret Sherry or Newton Sherry ever ask you to prepare those individual returns, is that correct?

(Testimony of Herndon Hughes.)

A. For '45 I am sure not, yes, sir.

Q. You didn't prepare the '46, did you?

A. That is right.

Q. So your answer is, as I understand it, you were not requested?

A. I am sure not, yes, sir.

Q. By them. Who did request you to prepare those returns, or your firm?

A. Well, things like this more or less happen, Mr. Carr. We were preparing the returns for the partnership, and during the course of the year you plan on what your estimate is going to be, and at the early part of the year 1945—and this again is my best recollection—neither of the children were present; neither of the children were here, and I am certain at the time that that estimate was filed and we got started into the return for the year 1945, that my conversation was exclusively with Mr. Sherry.

On the children's return I did—I mean upon their arrival back in Los Angeles I did talk to them, and to tell you that they never said anything to me about their individual returns I couldn't say that. That was just a growth from what we have been doing, and I prepared the returns. [14]

Q. Were you acquainted with whom it was that was operating the partnership, the S & P partnership? A. Yes, sir.

Q. Who?

A. Mr. Sherry and Mr. Paul Kalmanovitz.

Q. Paul Kalmanovitz? A. Yes.

(Testimony of Herndon Hughes.)

Q. And as far as the Sherry Enterprises partnership were concerned during the years 1944 and '45—I will stop there first; as far as you know, who was making the—who was managing the partnership?

A. Mr. Sherry, Nathan Sherry.

Q. Now we will come to 1946. To your knowledge did either one of the children participate in any way in the partnership in 1946?

A. Not to my knowledge, Mr. Carr.

Mr. Carr: May I have just one moment?

I think that is all.

Cross Examination

Q. (By Mr. Townsend): What would be the basis for your knowledge of whether or not these children——

A. My recollection here—I was just looking at the returns. The partnership return for the year 1946 is not here.

Q. I believe it is—— [15]

A. Oh, it is for the fiscal year ending June 30, 1946. I beg your pardon. Yes, it is here.

Mr. Townsend: May I have the question read?

(The question was read.)

Q. (By Mr. Townsend): ——participated in the operation of the Sherry Enterprises during the year '46 and the latter part of '45?

A. It would be my recollection, sir,—I don't recall that——

Q. My point is this, Mr. Hughes: Were you

(Testimony of Herndon Hughes.)

ever down in the office where they worked; were you ever down there fairly often or regularly?

A. Yes.

Q. Where you would observe what was going on?

A. Your questions here are regarding the Sherry Enterprises?

Q. That is correct.

A. The Sherry Enterprises was a—not an operating company in and of itself. The activities of the Sherry Enterprises were nominal indeed. There was no office for Sherry Enterprises, to my knowledge.

The Court: What was Sherry Enterprises?

The Witness: Sherry Enterprises, sir, was a copartnership which held the interest formerly belonging to Mr. Nathan Sherry in an operating partnership which in its later [16] years was nothing but the S & P Company.

The Court: What was that, a corporation?

The Witness: No, that was another partnership. Is my answer clear? May I——

Mr. Carr: Certainly, the Court asked you to explain it.

The Witness: The S & P was an operating partnership that had a number of restaurants and as I recall it in those days a bowling alley and several bars, and the operation of that company with a lot of employees and a lot of large office facilities. Mr. Nathan Sherry was at all times during the years here involved a co-partner of record in that partnership.

(Testimony of Herndon Hughes.)

The Court: The S & P?

The Witness: That is correct, but the Sherry Enterprises——

The Court: What was the scope of his interest in S & P?

The Witness: Fifty percent interest. He owned a 50 percent interest in S & P Company.

The Court: Who owned the other 50 percent?

The Witness: Mr. Paul Kalmanovitz.

The Court: Who are the partners in—was Sherry Enterprises an effort to divide up Mr. Nathan Sherry's 50 percent interest?

The Witness: It did in substance that, yes, sir.

The Court: Who were the partners in Sherry Enterprises?

The Witness: Mr. Nathan Sherry, Mrs. Nathan Sherry, Lucille Lawler Sherry, Margaret and Newton, the four members of the Sherry family.

The Court: Go ahead.

Q. (By Mr. Townsend): Mr. Hughes, you spoke that you were in on this forming the instrument for the partnership agreement and also preparing the gift tax returns and the donee tax returns.

Did Mr. Sherry state to you at the time what his purpose was in asking for those instruments?

A. Yes, sir. We had a discussion——

Mr. Carr: You mean Mr. Nathan Sherry?

Mr. Townsend: Yes.

A. I believe that the first discussion on this was probably in '43, Mr. Townsend.

In any event, the children were in the Service,

(Testimony of Herndon Hughes.)

and if it wasn't in '43 it was early in '44, and Mr. Sherry discussed at some length his family problems, his desire to protect the children, and as a result of those conferences the idea or the nucleus, his desire to protect them, the nucleus of the Sherry Enterprises was born and went from that to the attorney and from the attorney to the draft of the partnership form and back. [18]

Q. (By Mr. Townsend): Was there anything to lead you to believe that what was intended here was a sham partnership for tax purposes?

Mr. Carr: Well, I will have to object to that question. I think it is a little bit compound, complex, and I think he is entitled to state what was said. I don't want to be technical about it, but you are asking him——

Mr. Townsend: Was there anything said that would lead him to believe.

Mr. Carr: If you will leave out the word "sham" I think that——

Mr. Townsend: Let me try and rephrase the question.

Q. (By Mr. Townsend): Was anything said that would lead you to believe that this partnership was set up for tax purposes only?

A. The tax advantage was during the course of the conversations that ensued, discussed. The purpose of the corporation, as it was explained to me by Mr. Sherry—of the partnership, I am sorry—of the partnership as it was originally conceived and discussed with me by Mr. Sherry, Mr. Nathan

(Testimony of Herndon Hughes.)

Sherry, was an effort to divide his estate rather than income and protect his children by so doing.

Q. Give them a current interest in the business?

A. That would be my recollection.

The Court: Who suggested it, did you?

The Witness: No. [19]

The Court: Did your firm suggest it?

The Witness: No, sir. The suggestion initially came to me from Mr. Sherry himself, Mr. Nathan Sherry himself, as I recall it now, during a lunch. He was telling me of his effort to do something with his estate that would protect the children.

It started out actually talking about Newton who, I believe, was in the South Pacific at the time and he just had a letter from him, and that was the inception of the conversation.

The Court: Did you think in some way that you were effectively dividing up Mr. Nathan Sherry's 50 percent interest?

The Witness: Well, the attorney led us to believe that that is exactly what we were in effect doing.

Q. (By Mr. Townsend): Mr. Sherry also had income from other sources, didn't he, Mr. Hughes?

I believe if you look at your partnership return there you will find that there were additional sources besides the S & P partnership. I believe there was a corporation also, was there not, the S & P Corporation?

A. Gosh, was this '46 after the S & P was incorporated? I don't know.

(Testimony of Herndon Hughes.)

Mr. Carr: If I remember correctly, the S & P was incorporated in the latter part of '46 or some time around there. [20]

Mr. Townsend: Those returns speak for themselves and show other sources of income besides the S & P partnership; is that correct, Mr. Hughes?

The Witness: Yes.

Q. (By Mr. Townsend): Hollywood Cafe and a number of other items?

A. Yes, sir. In the year—we are calling it '46, it is actually the fiscal ending June 30, '46, there were several firms with which Mr. Sherry was associated reflected on the return.

The Court: Were they all partnerships or were they corporations or what were they?

The Witness: Your Honor, it has been so long; I recall that the Hollywood Recreation was a corporation. That's my recollection. Brooks Cafe was a partnership. C. R. Smith was a partnership. San Francisco was a partnership. And of course the big one was a partnership until Mr. Carr has just given you the date—it was a partnership up until —it must have been late in '46.

Do you know the date, Mr. Carr?

Mr. Carr: I don't know the date.

The Court: Did Mr. Nathan Sherry have a 50 percent interest in each one of these enterprises, whether they be corporations or partnerships?

The Witness: No. [21]

Mr. Carr: May I say one thing? It might clarify it. He had interests, a piece of this business, a piece

(Testimony of Herndon Hughes.)

of that business, 50 percent of this and 25 percent of this, which are not really involved here at all. But he had a 50 percent interest in S & P and he attempted to split that 50 percent four ways between the four members of his family, and the partnership Sherry Enterprises, namely, his wife, himself, and his two children, with a fourth each.

Mr. Townsend: I gather from these partnership returns that there is involved in the Sherry Enterprises more than the interest in the S & P Company.

Mr. Carr: Well, at varying times there was a sort of an in-and-out proposition. There would be some cafe in and then the next time some cafe out, but the major portion of the business—maybe I should put it this way—was the S & P partnership.

The Witness: The big portion——

The Court: May I have these exhibits, and will counsel please make other copies available to the witness so that I can follow this testimony?

Mr. Carr: Yes, your Honor.

The Court: Proceed.

Q. (By Mr. Townsend): Mr. Hughes, when you prepared these partnership returns, and I believe you prepared both of the returns that [22] are in evidence today, didn't you? A. Yes.

Q. Did you feel that this was a bonafide partnership when you prepared these returns?

A. Yes, sir.

Q. When you prepared these gift tax returns did you feel that a bonafide gift had actually taken

(Testimony of Herndon Hughes.)

place? A. Yes, sir.

Q. You did not feel at all that this was a fictitious partnership, did you?

Mr. Carr: I will have to object to what he feels. I think that is a question for the Court, your Honor. I object to it on the ground it calls for an opinion.

Mr. Townsend: I think this witness is well qualified to give that opinion.

The Court: He said he thought they were valid.

Mr. Carr: I will let it go that far, but I thought I ought to stop somewhere.

The Court: Mr. Hughes, some of these returns are signed by you and others are not, but your firm name appears to be stamped underneath the signature of some other person, apparently purporting to be associated with your firm.

Were all those returns prepared either by you or under your direction?

The Witness: Yes, sir. Paul Yessner is my partner, [23] your Honor.

The Court: So where his signature appears they are nevertheless prepared under your direction or in conjunction with you?

The Witness: Yes, sir.

The Court: Thank you.

Q. (By Mr. Townsend): Mr. Hughes, I show you what has been marked for identification as Respondent's Exhibit K and L and ask you to identify them, if you can, please.

Mr. Carr: You can just state what they are. I don't require you to lay a foundation.

(Testimony of Herndon Hughes.)

A. This Exhibit K is a report of an Internal Revenue agent on Mr. Newton Sherry's return for the year 1945, the report being dated September 9, 1948, made by Agent—I believe I can't tell you that.

Q. (By Mr. Townsend): Well, in summary, that is a revenue agent's report on the case of——

A. Newton Sherry for the year 1945.

Q. And on Margaret Sherry for the same year, which reflects adjustments to the Sherry Enterprises income and increases these petitioners' share of that income, is that correct?

A. That is correct, yes, sir. [24]

Q. Did you represent Newton Sherry and Margaret Sherry Ferguson at the time of this revenue agent's report and finding?

A. No, sir, I am sure I did not.

Q. This was with Revenue Agent Propeck, Mr. Hughes. Did you consult with him?

A. This was made in 1948.

Q. Correct.

A. I am sorry I haven't my file, but I am rather certain that I didn't have any of the records of Sherry Enterprises at this time.

You would be able to answer that question. I would have to say I don't think so, Mr. Townsend. I don't believe that——

Mr. Townsend: I have no further questions.

Mr. Carr: May I have just one further question?

Redirect Examination

Q. (By Mr. Carr): May I ask if anything you

(Testimony of Herndon Hughes.)

did do on behalf of Margaret or Newton Sherry was at the request of Mr. Nathan Sherry?

A. That would be completely so, with the possible exception of their individual return for the year—the last return I prepared.

Now, the children were back by that time, Mr. Carr, and I talked to the children and——

Q. You didn't prepare the '46 return though, did you? [25]

A. I don't believe I did.

Q. Well, that is what I am asking. You take a look.

A. May I ask you, when did the children come back?

The Court: You may not ask counsel questions.

The Witness: Then I can't answer with definite knowledge.

Q. (By Mr. Carr): Look at the return for the fiscal year.

A. But I couldn't tell whether I discussed anything on that with them by looking at it.

Q. You can tell whether you prepared it?

A. I certainly did prepare the return.

Q. Look at your '46 return. Did you prepare that for the two children?

A. No, sir, the '46 I did not prepare.

Q. That is the fiscal year ending——

A. This is for the children now you are talking about?

Q. That's right, for the children.

(Testimony of Herndon Hughes.)

A. No, sir, I did not prepare the children's return for '46.

Mr. Carr: That is all. No further questions.

Recross Examination

Q. (By Mr. Townsend): The 1945 return which you did prepare for the children was of course filed on March 15, 1946? [26] A. Yes, sir.

Q. Could that be the return that you have been referring to?

A. I wouldn't say that I did not discuss anything with respect to the children's return after they came back to the city; I probably did. But it was Mr. Newton Sherry that had instructed us to originally proceed.

Mr. Townsend: I have no further questions.

The Witness: I mean Mr. Nathan Sherry.

Further Redirect Examination

Q. (By Mr. Carr): I hate to keep doing this, but to refresh your recollection, don't you recollect that Margaret Sherry did not return from the Service until November of 1945?

A. I don't remember when she came back, Mr. Carr.

Q. Do you recollect that Mr. Newton came home from the Marines in May 1945 and went into a hospital?

A. I don't think I saw Newton until after he got out of the hospital, and I don't know what the date was when either of them got back.

(Testimony of Herndon Hughes.)

Q. But you didn't discuss, I take it, then, anything with either one of them until their return from the Service?

A. Some weeks after they got back to town.

Mr. Carr: That is all.

Mr. Townsend: That is all. [27]

Mr. Carr: May he be excused, your Honor?

Mr. Townsend: Yes.

The Court: You may be excused.

(Witness excused.)

Whereupon,

NEWTON SHERRY

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

The Clerk: State your full name and address, please, Mr. Witness?

The Witness: I didn't hear you.

The Clerk: State your name and address, please.

The Witness: Newton Sherry, 2210 Graham Avenue, Redondo Beach.

Direct Examination

Q. (By Mr. Carr): What is your occupation?

A. I am a painter.

Q. What kind of painter?

A. House painter.

Q. You work for wages?

A. That is right.

Q. And how old are you?

A. I am 37. [28]

(Testimony of Newton Sherry.)

Q. Do you hear well? A. Not too well.

Q. As a matter of fact, you more or less read lips, don't you? A. That is right.

Q. To understand.

I bring it out, counsel, so if you will face him when you talk to him.

Now, Mr. Sherry, do you remember a partnership agreement that you signed setting up Sherry Enterprises?

A. Well, as far as that goes, the only one that I remember was signing overseas.

Q. Where were you at the time you signed this agreement?

A. I was at Guadalcanal at the time.

Q. I will use this copy, your Honor, and I am referring now to Exhibit—this is the petitioner's exhibit; that is Exhibit G, I believe. Is that your signature, Mr. Sherry? A. That's right.

Q. Where were you at the time you signed that?

A. At Guadalcanal.

Q. What were you doing there at Guadalcanal?

A. Well,——

Q. What was your business? I don't mean what were you doing at the moment. What was your business?

A. Oh, I was a Sergeant in the Marine Corps.

Q. And you say you signed that?

A. That's right.

Q. Did you read the agreement when you signed it? A. Not particularly.

Q. Well, did you or didn't you?

(Testimony of Newton Sherry.)

A. No, I didn't.

Q. Well, who asked you to sign the agreement?

A. My dad sent me a letter for me to sign it.

Q. And you signed it? A. Yes.

Q. What did you do with it, mail it back to him?

A. That is right.

Q. Now, when did you return from the Marine Corps?

A. It was about March of 1945, and then I went to the hospital, and I was transferred to the Philadelphia Hospital.

Q. How long was it before you returned to Los Angeles?

A. It was—well, it wasn't until about May 1945.

Q. In the meantime you had been, on your return to the country, you had been in the hospital?

A. That is right.

Q. Incidentally, is that during the time you were looking to lip read? A. That is right.

Q. Now, do you remember signing any tax returns for the Sherry Enterprises? [30]

A. No, sir, I don't.

Q. Let me show you your signatures here and see if you recognize them.

By the way, you were married to Lois Sherry when? A. In 1940, January.

Q. Are you living together now or separated?

A. No, we are separated.

Q. Do you have any children?

A. Well, not by her.

Q. How many children do you have?

(Testimony of Newton Sherry.)

A. I have four.

Q. Four children.

Now, I want to show you Exhibit C. Is this your signature? No, that is not the one. Just a moment. Is that your signature?

A. That looks like it. I believe it is.

Q. Do you know whether or not your father signed your name at any time to any of these things?

A. I checked some signatures over, and I know that he signed one of them.

Q. Which one, do you know which one he signed?

A. No, sir, I don't.

Q. Now, do you recollect signing a tax return for 1944 for yourself individually, that is, you and your wife, for 1944? [31]

A. I can't recall, I am sorry.

Q. Do you remember signing one for 1945?

A. No, sir.

Q. Do you remember signing one for 1946?

A. I don't remember, no, sir.

Q. Now, I will show you the return which is Exhibit B for 1946. I take it—there is an "X" by that Newton Ivan Sherry. Is that your signature?

A. It looks like it, yes, sir.

Q. You think you signed that one?

A. I believe so.

Q. Do you know where you got that return to sign it?

A. Oh, it has been so long ago, I mean I couldn't recall.

(Testimony of Newton Sherry.)

Q. Let me ask you this: Do you remember signing—when it was you signed the partnership agreement? You say it was in Guadalcanal?

A. Yes, sir.

Q. Remember about when it was?

A. I believe it was in 1943 or '44, somewhere in there.

Q. Did you ever at any time receive any funds from the Sherry Enterprises partnership?

A. No, sir.

Q. Not a nickel? A. No, sir. [32]

Q. Did you ever at any time pay any taxes, as far as you know, to your own knowledge, on any income for the Sherry Enterprises?

A. No, sir.

Q. Or for your share of it?

A. That is right.

Q. You don't remember ever paying any?

A. No, sir.

Q. Did you ever ask anyone to prepare a partnership agreement? A. No, sir.

Q. Did you ever ask anyone to prepare tax returns for you?

A. No, sir, not during that period of time.

Q. I am talking now about 1944, '45, '46.

A. No, sir.

Q. Just what did you know about the Sherry Enterprises?

A. Actually, I didn't know anything.

Q. Mr. Nathan Sherry, I believe, was your father? A. That's right.

(Testimony of Newton Sherry.)

Q. And when had you joined the Marine Corps?

A. In 1940, January.

Q. 1940? A. Yes, sir.

Q. And you were discharged when? [33]

A. 19—May of 1945.

Q. Now, during the time that you were back in Los Angeles did you work for your father at any time? A. I did.

Q. Where did you work?

A. I worked at the Bayview in Wilmington.

Q. Wilmington, California?

A. That is right.

Q. What was that?

A. It was a, well, combination, a drive-in and bar.

Q. Do you know who owned that?

A. I believe it was Mr. Paul and my dad.

Q. Who is that?

A. Paul Kalmanovitz.

Q. Paul Kalmanovitz? A. Yes.

Q. And your father—you think they owned it?

A. It was S & P, I am sure.

Q. Did you get a salary while you worked there?

A. I got a manager's salary.

Q. How much salary did you get?

A. I believe it was about $110.00.

Q. For what period? A. For what——

Q. For what period, a week, a month, or what?

A. No, that was a week.

Q. And did you have anything to do with making out the books and records?

(Testimony of Newton Sherry.)

A. No, sir.

Q. Did you have anything to do with the income tax returns for that particular business where you worked?

A. No, sir, they were all turned in.

Q. Who handled that?

A. They had an office up on Vine that handled all that.

Q. Did you have anything to do with the office on Vine Street? A. No, sir.

Q. Didn't you go to school for a while after you got out of the hospital?

A. I did. That was after I was discharged in May of 1945.

Q. By the way, what does your former wife do? Are you divorced from Lois Sherry?

A. No.

Q. What does she do, do you know?

A. She works as an I.B.M. operator at Michigan Gas & Appliance.

Q. When did you get out of college, when did you finish this college course?

A. Well, I actually didn't complete it. My dad called [35] me down and wanted me to participate in being a manager at the Bayview.

Q. At the Bayview in Wilmington?

A. In Wilmington, yes, sir.

Q. When was that, do you remember about when it was?

A. Well, it was right after I was—I quit school. I had some paper to that effect of when I quit

(Testimony of Newton Sherry.)

school, because that was the reason why I quit college at that time.

Mr. Carr: Do you want to see these, counsel? His college papers showing his attendance there?

The Witness: I never did receive any grades or anything.

Mr. Carr: Just for purposes of refreshing his recollection to get a date.

Q. (By Mr. Carr): I will show you here what purports to be a California State Polytechnic record. Do you recognize that? A. Yes.

Q. See if that refreshes your recollection, if you can remember the date after looking at it.

A. It would be about the eleventh month of 1945, in other words, that I went to work at the Bayview.

Q. Eleventh month, you mean November?

A. Yes, sir.

Mr. Carr: No further questions. [36]

Cross Examination

Q. (By Mr. Townsend): Can you understand me from here, Mr. Sherry? A. Yes, sir.

Q. I believe you testified that your father sent you that partnership agreement along with a letter?

A. That's right.

Q. That you didn't read the partnership agreement, but I presume you read the letter?

A. Yes. He just in the letter informed for me to sign some papers.

Q. What did he tell you the papers were for, in the letter? A. To tell me what?

(Testimony of Newton Sherry.)

Q. What did he tell you the papers were for in his letter?

A. Well, he didn't actually state in the letter what they were for.

Q. He didn't tell you in the letter that he was setting up a partnership? A. No, sir.

Q. He just said in his letter, "Here are some papers, sign them?" A. Yes, sir.

Q. He didn't say anything about he wanted you to go into [37] business with him when you came out of the Marine Corps? A. No.

Q. Or he wanted to protect your future?

A. No, sir.

Q. He said nothing in this letter about it?

A. No, sir.

Q. And you just took this document and signed it? A. Yes, sir.

Q. Now, when did you first find out about the partnership?

A. Well, a while after I got back, in other words, when I got discharged from the Service, then I went to school, and then it was at a later date that I heard that I had had some word that there was a partnership.

Q. Could you go a little more into detail? How did you get the word and when?

A. I had heard it discussed between Mr. Paul and my dad.

Q. You heard the Sherry Enterprises discussed between Mr. Paul and your dad?

A. Yes, sir.

(Testimony of Newton Sherry.)

Q. Now, have we identified exactly which returns you signed there, your individual returns?

A. Well, actually, I don't remember all these.

Q. Excuse me. Let me pick them out for you here.

A. In other words, he brings something in and says, "Sign this." I'd sign this, you know, you trust your dad that [38] way.

Q. Referring to Exhibits C and D, which purport to be your individual income tax returns for 1945 and 1946, are those your signatures on both of them? A. I believe they are, sir.

Q. You did sign them. Now, you looked at those returns when you signed them, didn't you, Mr. Sherry?

A. I don't remember looking at anything that I signed, as far as that goes, because if he'd tell me to sign something I'd sign it.

Q. You knew it was an income tax return, didn't you?

A. No, sir, a lot of times I didn't.

Q. Let's look at those two particular ones. How about when you signed those, did you know what they were?

A. He'd put it in front of me and tell me to sign it, like that.

Q. You knew what you were doing when you signed that return, didn't you?

A. Well, what I was doing in signing that, no, sir. I mean he put a lot of things in front of me and would tell me to sign it, I'd sign anything. It

(Testimony of Newton Sherry.)

is just like buying an automobile, you don't read everything.

Q. You knew that that return was going to be filed with the government, didn't you?

A. No, sir, I didn't. [39]

Q. Had you ever heard of the income tax laws before? A. No, sir.

Q. You received a salary, I believe, in 1946 from the S & P Company, didn't you, Mr. Sherry?

A. To whom?

Q. From the S & P Company?

A. In what year?

Q. In 1946? A. That's right.

Q. You intended to report that income, didn't you, to the government? A. Yes, sir.

Q. Did you make some effort to find out whether that income had been reported or not?

A. Well, my dad, in other words, I followed everything, then Murray made those out.

Q. You knew what that was, didn't you, this one prepared by Mr. Murray, your 1946 return; you knew what that one was?

A. If I filled it out, I knew what it was.

Q. Let's take a look at it right there.

A. A lot of these I didn't have nothing to do with filling out anything.

Q. You were interested in reporting your salary from S & P Company, weren't you? [40]

A. That's right.

Q. You intended to do that?

(Testimony of Newton Sherry.)

A. I am interested in what I make as a partner now.

Q. This '46 return, Exhibit D, shows your salary from S & P Company of $1,950.00. You knew you were reporting that, didn't you?

A. If it states that I imagine so.

Q. You looked at that particular return, didn't you? A. This was by Murray.

Q. You looked at that particular return, didn't you?

A. I don't remember whether I looked at it or not, because he might have filed it with him. In other words, just about all the business was done by my dad, in fact, everything was.

Q. Weren't you concerned with whether or not your income from S & P Company was reported to the government?

A. In that fact, I consulted my dad on it, on my income from S & P Company.

Q. And you made certain steps to make sure that that income was reported, did you not, the salary that you got?

A. That is right, in other words, he said that it was reported and I just signed.

Q. You looked at the report, did you not, to see if it included that salary?

A. I don't remember whether I did or not. [41]

Q. You don't remember whether you looked at the return or not when you signed it?

A. No, sir.

Q. So far as you know, I take it, so far as your

(Testimony of Newton Sherry.)

testimony goes, you don't know whether or not you ever reported any income from this partnership or from any other source, is that correct?

A. You are turning it around a little bit. I remember reporting what I have made since then, when I painted, I mean. Everything else was handled by him.

Q. Did you ever conduct any businesses for the Sherry Enterprises?

A. No, not actually, not conduct them myself.

Q. What did you do exactly when you came back from Guadalcanal?

A. When I came back from Guadalcanal?

Q. That's right.

A. I worked at the—I went down and worked at the Bayview for a while, and then I went back to painting for a while. Let's see, and after—I remember one business that I wasn't running that I was sent down to work at.

Q. What was that?

A. Well, that was at Miami. I was a laborer down there.

Q. What was the name of that business?

A. Oh, that was in later years. [42]

Q. Did you have anything to do with the Le Fleur de California? A. Yes.

Q. What was that?

A. That was established as a—Le Fleur was a perfume outfit.

Q. Right, and what connection did you have with that business?

(Testimony of Newton Sherry.)

A. Well, I participated and worked there myself.

Q. What connection did your father have with that business?

A. Well, it was his business, as far as that goes.

Q. Was that——

A. Anything that I was engaged in, I mean, he told me, "Do this, do that, you are in this, you are in that."

Q. Did you ever have meetings of the four family members that signed that partnership agreement? A. Not that I recall.

Q. Did you ever have meetings in which business policies and plans were discussed?

A. No, sir, he never discussed anything with me, to speak of. I mean he is very close mouthed about business.

Q. You purchased a home in 1946, did you not?

A. 1946? Let's see, I believe so.

Q. For $8,599.00, correct? [43]

A. That's right.

Q. Where did you get that money?

A. Well, he gave me the money, but it was returned to him afterwards, after it was sold. What year was that?

Q. 1946.

A. '46? It would be about that time. That was when I was working at the Bayview, as I recall.

Q. Did you ever do any work for Linda Gale, Incorporated? A. What date was that?

Q. I don't know, Mr. Sherry.

(Testimony of Newton Sherry.)

A. Wasn't that at a later date?

Q. I don't know. I am asking you.

A. I believe that was in the year 1949.

Q. 1949, and who owned that company?

Mr. Carr: I object to going into 1949 unless it is a part of the partnership to reflect back. I don't see how it would have any bearing, your Honor. To me we are going into collateral matters.

The Court: What is the connection?

Mr. Townsend: I believe that subsequent events are admissible to show the intention of these parties back in these early years.

The Court: If you can tie it in, I will let you attempt to do so. [44]

Q. (By Mr. Townsend): What was Linda Gale, Incorporated?

A. Linda Gale, Incorporated? It was a partnership set up by Mr. Klein.

Q. What connection did your father have with it?

A. Well, my dad—my dad and Mr. Klein set it up in a business for me to work in it.

Q. Was that considered one of the assets of the Sherry Enterprises?

A. In a later date, yes.

Q. How about your home, was that considered to be your own asset or was that considered an asset of Sherry Enterprises?

A. What home?

Q. The home you purchased in 1946 for $8,599.00?

(Testimony of Newton Sherry.)

A. That would have been Sherry Enterprise at that time.

Q. You didn't consider it your house?

A. No, sir.

Q. When did you consider yourself, if you ever did, a partner in Sherry Enterprises?

A. When did I consider myself a partner?

Q. Yes, or did you ever? A. I never did.

Q. You never considered yourself a partner?

A. No, sir.

Q. In Sherry Enterprises?

A. That's correct. [45]

Q. Did you have anything to do with the Martin Holding Company?

A. I don't recall that.

Q. The Martin Holding Company?

A. No, sir.

Q. You recall nothing about it?

A. No, sir.

Q. I show you what has been marked for identification as Respondent's Exhibit K, which is a waiver of restrictions on the assessment and collection of deficiency in tax, and ask you if that is your signature thereon.

A. Yes, sir, that is my signature.

Mr. Carr: I didn't hear the answer. What did he say?

Mr. Townsend: He said it was.

Q. (By Mr. Townsend): You will notice the date that that is signed?

A. July 19, 1948.

(Testimony of Newton Sherry.)

Q. What were the circumstances when you signed the particular instrument?

Mr. Carr: I am not objecting to this on the theory that you are going to connect it up. I assume that you will.

A. What were the circumstances?

Q. (By Mr. Townsend): Yes.

A. Most of this, I mean, it is—the same as that, [46] it's the same difference, what I am speaking about. I signed things a lot of times that I didn't know what they involved or anything else.

Q. Did you know when you were signing this that you were agreeing to an additional deficiency in tax of $1,114.00?

A. I don't remember that.

Q. You don't remember that?

A. No, sir.

Q. Who told you to sign that?

A. My dad.

Q. When did your father die, Mr. Sherry?

A. When did he die?

Q. Yes.

A. It has been about, let's see, he died in January, about two years ago.

Q. Mr. Sherry, do you recall coming down to this building on November 2, 1949 with your attorney, Conrad Hubner and Mr. William Byrns, a special agent was here at that time. Do you recall that incident?

A. About seeing Mr. Byrns?

Q. That's right, in this very building.

(Testimony of Newton Sherry.)

A. Oh, very well. I remember Mr. Byrns. He got mad at me at that time.

Q. Do you recall that you gave a question-and-answer statement at that time? [47]

A. I remember he asked me some questions. I don't recall what questions they were.

Q. You remember that you testified under oath at that time, do you not? You remember being sworn in?

A. I don't remember whether he swore me in or not, sir.

Q. Were the answers that you gave at that time true and correct, as far as you knew then?

A. Well, it's just like trying to think back when you were a child or something. I mean I can't remember years back or five years or three years or something, I mean——

Q. In 1949 when you saw Mr. Byrnes and he asked you these questions, did you answer them truthfully, to the best of your ability?

A. The best of my ability, I imagine so.

Q. You didn't lie, did you? A. No, sir.

Q. Now, at that time that Mr. Byrnes was asking you questions, do you recall this question being asked and this answer being given by you:

"Q. Are you a partner in the partnership known as Sherry Enterprises? A. I am."

A. At that time I guess, if that's what is in there, well,——

Q. So at that time in January of 1949 you ap-

(Testimony of Newton Sherry.)

parently [48] felt that you were a partner in Sherry Enterprises? A. That's right.

Q. But just a few moments ago you said that you had never considered yourself a partner in Sherry Enterprises?

A. Well, considering yourself and participating and receiving funds out of it that you can take and put in the bank and keep, it's a different thing.

Q I am just talking about what you considered and when you considered yourself a partner.

A. Well, I was no active partner.

Q. I am not asking you that. I am asking you when you considered yourself a member of Sherry Enterprises.

A. Just like I said in court a few minutes ago, I found out that—I was part of Sherry Enterprises as set up.

Q. When?

A. After I got out of the Service, and then when I came down to participate in the business.

Q. And that would be the end of '45, would you say?

A. No,—it was approximately at that time, yes.

Q. But during that time and for there on in you considered yourself then a member of Sherry Enterprises partnership?

A. You turned it around a certain way, but considering yourself and being a partner is two different things.

Q. I agree, it is up to the Judge to determine

(Testimony of Newton Sherry.)

that point. [49] We are just asking what you consider.

A. Well, I never actually considered myself at any time a partner, what you call a partner in anything.

Q. Then why did you tell Mr. Bryns in 1949 that you were a partner?

A. Because it was wrote up as a partnership.

Q. But the question asked was, "Are you a partner in the partnership known as Sherry Enterprises?"

According to you right there a few minutes ago, you said yes. A. That I said "Yes"?

Q. That right, you said, "I am."

A. "I am."

Q. At that time then apparently you felt yourself a bonafide member of that partnership?

A. Well, I don't know. I always thought a partnership was something different than what that was.

Q. You knew the reason that you were being asked questions on that answer-and-question statement? A. What?

Q. You know the reason why you were called down at that time and asked those questions under oath, don't you?

A. Not particularly, I mean I don't believe I recall.

Q. Do you recall that your father was being investigated at that time? [50]

A. I have heard something to that effect, yes.

Q. And you knew that at the time you came

(Testimony of Newton Sherry.)

down here and answered these questions, did you not? A. I believe so.

Q. And you also knew that at that time it would help your father if there was a partnership known as Sherry Enterprises?

A. I didn't know that.

Q. You didn't have that thought in mind when you answered these questions? A. No, sir.

Q. Was any of your money ever contributed to Sherry Enterprises? A. What?

Q. Was any of your money ever contributed to Sherry Enterprises?

A. To Sherry Enterprises?

Q. Yes.

A. Well, when my mother passed away, there was at that time.

Q. How much was that, Mr. Sherry?

A. Well, I never had the money in my hand or anything, but I heard that it was $20,000.00, I believe. I know when I was a child that I went down to the bars that she had at that time. [51]

Mr. Carr: I will have to move to strike that on the ground that it is hearsay, your Honor, what he heard.

The Witness: That was just S & P, that wasn't Enterprises.

The Court: The Court will not consider any hearsay testimony.

Mr. Carr: I didn't think that you would, so I just——

(Testimony of Newton Sherry.)

Q. (By Mr. Townsend): Did you ever invest any money yourself in Sherry Enterprises?

A. I never had any money to invest, sir.

Q. Mr. Sherry, referring again to the date that you were down here on November 2, 1949, when Mr. William Bryns was interviewing you under oath, do you recall this question being asked you and your answer as follows:

"Q. In your opinion, what was the purpose of the formation of Sherry Enterprises partnership.

"A. Well, the formation, in other words, is between all of us. The money was put in in case anything should happen to my dad, we would still have a partnership. Also, there was money that was left to us that made up the partnership. Also, there was money I invested that made up the partnership."

Do you recall that question and that answer, Mr. Sherry? [52]

A. No, sir, it's been so long ago.

Q. Do you deny that now?

A. No, sir, I won't deny it.

Q. Those facts I am talking about?

A. Well, over a period of years people, you know, they forget things unless your mind is a photographic mind, like some people have.

Q. Well, let's just take the one part. "Also, there was money I invested," that made up the partnership, is that true or not? A. It what?

Q. "Also there was money I invested that made up the partnership;" is that true or not?

A. Well, the part that may be—participating to

(Testimony of Newton Sherry.)

"I invested" would have been the money left through my mother at an earlier date, I imagine.

Q. Let me read you that sentence again, "Also, there was money that was left to us that made up the partnership. Also, there was money I invested that made up the partnership."

A. I don't remember investing any money, sir. Sometimes people ask you questions and it is rather confusing the way Mr. Bryns asked me those questions. They turned them all around and all.

Q. Do you recall this question being asked you on the same date, which is November 2, 1949, by Mr. Byrns and your [53] answering as follows:

"Q. Since the formation of Sherry Enterprises has there ever been a meeting of all the four partners in which business policies and plans were discussed?

"A. Well, at different times, if ever we wanted any type of business whatsoever added to the Sherry Enterprises, we would all get together and have a mutual agreement."

A. I don't remember stating that. I could have stated it, but I don't remember us getting together, to speak of.

Mr. Townsend: No further questions.

Mr. Carr: May I just ask one or two short questions?

Redirect Examination

Q. (By Mr. Carr): Mr. Nathan Sherry, your father, was a very aggressive man, wasn't he?

A. What?

(Testimony of Newton Sherry.)

Q. Aggressive man. A. That's right.

Q. And when he spoke to you, did he ask you to do something or tell you to do something?

A. He told me to do it.

Q. And did you do what he told you to do?

A. I always did, yes, sir. [54]

Q. No matter what it was?

A. No, sir, didn't matter what it was.

Q. If it were wrong, would you do it too?

A. I would still do it. I happen to love him that much.

Q. Your father and you were very close, weren't you? A. How is that?

Q. Your father and you were very close?

A. Speaking that way, I mean, as far as love for him it was close that way.

Q. Did he ever tell you anything about what he was doing in business?

A. No, sir, not to my knowledge.

Q. By the way, one other question. Your dad was later, do you remember, indicted some time after that statement was given? You know what "indicted" means, prosecuted in the Federal Court for tax evasion? A. Yes, sir.

Q. Mr. Byrns was a special agent who was investigating him at that time, is that correct?

A. Well, it must have been Mr. Byrns because that was the one that I came down to see there one time.

Mr. Carr: I think that is all.

Mr. Townsend: I have no further questions.

The Court: We will reconvene at 2:00 o'clock.

(Whereupon at 12:15 p.m., a recess was taken until 2:00 p.m. of the same day.) [55]

Afternoon Session—2:00 p.m.

The Court: Have these cases been consolidated?

Mr. Townsend: No, they have not.

The Court: Does counsel wish to make a joint motion for this purpose?

Mr. Carr: Yes, we join in the Court's suggestion and move that they be consolidated.

Mr. Townsend: The respondent so agrees.

The Court: The cases will be consolidated, and the evidence received thus far will be treated as having been received in the consolidated hearing.

Mr. Townsend: So stipulated.

Mr. Carr: So stipulated.

Whereupon,

MARGARET FERGUSON

called as a witness for and on behalf of the Pettioner, having been first duly sworn, was examined and testified as follows:

The Clerk: State your name and address, Miss Witness. You may be seated.

The Witness: My name is Margaret Ferguson. I live at 1810 Courtney Avenue, Los Angeles 46.

Direct Examination

Q. (By Mr. Carr): Mrs. Ferguson, you were formerly Margaret Sherry, [56] is that correct?

A. That is correct.

(Testimony of Margaret Ferguson.)

Q. You are the daughter of the deceased, Nathan Sherry? A. That is correct.

Q. Now, I want to draw your attention particularly to the years beginning about 1943 and through the years up until the fiscal period ending June, 1948.

First of all, where were you in February of 1943?

A. I went into the Service in February, 1943.

Q. What branch of the Service?

A. The Navy.

Q. You mean the Waves?

A. That's right.

Q. How long were you in the Waves?

A. Almost three years.

Q. When did you go in?

A. February, 1943 and I was in until November, 1945.

Q. November, 1945? A. That's right.

Q. Now, do you recollect having signed a partnership agreement, I will place it before you, that is Exhibit G. I will show you there a signature. Is that your signature? A. Yes, Mr. Carr.

Q. Who asked you to sign that?

A. My father. [57]

Q. Where did you receive that request?

A. I was still in Los Angeles when this partnership agreement was made—no—no. I was in the Navy, that's right.

Q. Well, how did you get it to sign it?

A. Through the mail.

Q. How did you get it?

(Testimony of Margaret Ferguson.)

A. Through the mail.

Q. Through the mail, and who sent it to you?

A. My father.

Q. And did you read the agreement?

A. I don't remember reading it.

Q. Did he request you to sign it, or what did he say to you?

A. He wrote—well, I really don't recall what he said. He undoubtedly sent me a letter with it telling me to sign the papers and return them.

Q. Where were you at that time, by the way?

A. Dayton, Ohio.

Q. And did you come home from time to time?

A. I had two leaves during the three year period.

Q. Now, at any time while you were on leave did you undertake to manage any of this—these partnership assets or do anything about them? [58]

A. No, sir.

Q. Were you consulted at any time by the other alleged partners to this agreement, to-wit: your stepmother, Mrs. Sherry, or Mr. Sherry, your father, or your brother? A. No.

Q. Until you returned here in November of 1945, did you ever attend a meeting with anyone in which you discussed the management of this Sherry Enterprises? A. No.

Q. Did you ever have any correspondence with your father about policy or management of Sherry Enterprises? A. No, sir.

(Testimony of Margaret Ferguson.)

Q. Do you recollect signing Exhibit—withdraw that.

Did you request anyone to make up a partnership return for Sherry Enterprises for 1945 or '46?

A. No, sir.

Q. Do you know who did? Did you ever get a copy of the partnership returns for those years?

A. No.

Q. Do you recollect ever having seen a copy of the partnership returns for the years, fiscal years 1945 and '46? I am talking about now up to the trial, not since that time.

A. Are you talking about income tax returns?

Q. Yes.

A. They were sent to me. [59]

Q. No, I am talking about the partnership returns. A. Oh, no, no.

Q. Do you ever remember seeing the partnership returns? A. No.

Q. Now, then, did you receive some individual returns for yourself? A. Yes.

Q. For those two years? A. Yes.

Q. And was that on a calendar year basis, do you know? A. No, I don't.

Q. Do you know what I mean by "calendar year"? A. No, not specifically.

Q. As distinguished from a fiscal year ending June 30th?

A. January to January, or June to June?

Q. January to December 31st would be your cal-

(Testimony of Margaret Ferguson.)

endar year. Was that the basis on which you reported your return?

A. I don't remember.

Q. Now, did you request anyone to prepare your individual returns for the year 1945 and the year 1946? A. No.

Q. How did you receive them?

A. I received them through the mail.

Q. From whom?

A. From my father. [60]

Q. And did you go over them?

A. I remember looking at them. I didn't——

Q. I show you here, in the meantime, I now have the gift tax returns, Exhibits J and I, and I notice the signature here, do you remember signing as donee the gift tax returns?

A. I don't recall.

Q. Do you ever remember getting the gift tax returns? A. No.

Q. Do you ever remember having a discussion at any time with anyone about the formation of the partnership? A. Before it was formed?

Q. Yes. A. No.

Q. Did your father ever mention to you before it was formed that he was forming a partnership?

A. No.

Q. The first notice, then, I take it, you got was when you got the partnership document from him asking you to sign it, is that right?

A. That's right.

Q. I show you here Exhibits I and J which

(Testimony of Margaret Ferguson.)

are the gift tax returns. I take it those are your signatures, aren't they? A. They are.

Q. Do you remember now where you signed those as donee? A. No. [61]

Q. You have no recollection? A. No.

Q. Do you remember whether your father asked you to do it or someone else?

A. My father would have asked me to do it.

Q. Do you remember ever having looked into those returns to see what they contained?

A. No.

Q. Now, I will show you next your income tax returns for the years '45 and '46. This is Exhibit A and Exhibit B. Exhibit A is for 1945, and let's see if this is your signature. Is that it?

A. That is it.

Q. Now, do you recollect going over that to check the figures?

A. No, I remember that I looked at them, but the figures didn't mean anything to me.

Q. From whom did you receive that?

A. From my father.

Q. By mail? A. Yes.

Q. And where were you at the time?

A. In Dayton, Ohio.

Q. Now, I show you Exhibit B and ask you the same [62] series of questions, first as to signature?

A. It is mine.

Q. Do you remember receiving that?

A. Yes.

Q. How? A. Through the mail.

(Testimony of Margaret Ferguson.)

Q. From whom? A. My father.

Q. Did you go—look into it to see if it was correct?

A. I would have had no way of knowing whether it was correct or not. No, I didn't.

Q. What did you do with those two, A and B? What did you do with these two exhibits?

A. I signed them and returned them.

Q. To whom? A. My father.

The Court: Where were you when you received Exhibit B?

The Witness: In Dayton, Ohio.

The Court: When were you mustered out of the Navy?

The Witness: November, 1945.

Mr. Carr: This is Exhibit A she was talking about, your Honor.

Q. (By Mr. Carr): Now, Exhibit B, I assume the Court wants to ask [63] you the same question.

The Court: I asked her about Exhibit B.

Mr. Carr: I am sorry.

The Witness: The date on this was what? February 6, 1947. In that case I would have been in Los Angeles.

Q. (By Mr. Carr): You were in Los Angeles at that time?

The Court: Are you guessing or testifying from your actual recollection?

The Witness: I was in Los Angeles in 1947.

The Court: Well, then, how did you receive Exhibit B?

(Testimony of Margaret Ferguson.)

The Witness: Then, it was undoubtedly given to me by my father at home. I got all the income tax returns——

The Court: Did you live with your father then?

The Witness: Yes.

Q. (By Mr. Carr): So, then, you got Exhibit A through the mail, you say?

A. Yes—well, there is no date on this one. If it was 1945, I must have gotten it through the mail.

Q. Well, it was for the calendar year 1945?

A. Yes, that's right. I received it through the mail.

Q. When did you get back to Los Angeles?

A. November, 1945.

Q. Isn't it a fact you have been here in Los Angeles in 1945? [64]

A. No, because it says on this income tax return I was in the United States Navy. I couldn't have been at home.

The Court: Do you know when Exhibit A was signed?

The Witness: Do I know the actual date that I signed it?

The Court: Suppose you look at the date that appears opposite your signature.

The Witness: March 8, 1946. Is that right? Is that the date on the return?

Mr. Carr: That is right. That is correct.

The Court: That doesn't seem to be the date that pertains to her signature. The one that per-

(Testimony of Margaret Ferguson.)

tains to *be* her signature is to the right of her signature.

The Witness: No, then, I would have been in Los Angeles 1946.

Q. (By Mr. Carr): That is what I am getting at. So, you were here when both of those were signed, weren't you? A. I——

Q. You were out of the Navy at that time?

A. I was in 1946.

Q. So, you were in error when you said you got those through the mail?

A. I did get some in the mail while I was in the Service. I thought these were the ones. [65]

Q. Did you ever get a copy of the partnership returns? A. Not that I recall.

Q. Did you get the partnership agreement through the mail? A. Yes.

Q. Now, are you sure about that, or did you sign that before you went away to the Service?

A. Well, the date on it is October, 1943, and I was in the Service in October, 1943.

Q. All right. Now, what, if anything, did you do to help manage this partnership when you came back from the Service? A. Nothing.

Q. Well, you say "nothing." Didn't you do some errands for your father?

A. Oh, of course.

Q. Did you go to the bank sometimes for him?

A. Yes.

Q. Did you go cash checks for him?

A. Sometimes.

(Testimony of Margaret Ferguson.)

Q. Weren't you on the—allowed to sign checks on the partnership? I am talking about Sherry Enterprises now. Couldn't you draw a check on that?

A. Yes. We had joint bank accounts, my father and I, which I assume were part of the Sherry Enterprises, Mr. Carr. [66]

Q. Did you draw checks on that to pay for anything?

A. Household expenses, yes.

Q. Whose household expenses?

A. My father's and mine, we lived together.

Q. Did you do any errands for him in connection with the partnership, Sherry Enterprises?

A. I'd make deposits for him.

Q. What else would you do?

A. That is about all.

Q. Now, did you have anything to do with setting the policy of the partnership, Sherry Enterprises? A. No.

Q. Did your father discuss with you the management or setting of policy of that partnership?

A. He would sometimes tell me what he was doing, but I had no opportunity to voice an opinion about it.

Q. Did you ever have, to your knowledge, a formal meeting which was attended by your brother, your father, and your stepmother to discuss matters of partnership?

A. A formal meeting? No.

Q. Well, maybe the word "formal" is a bad word. Did you have a meeting in which all four

(Testimony of Margaret Ferguson.)

of you sat down and discussed policy relating to the partnership?

A. The only times we ever discussed it with all members present would be at a dinner, something of that kind. [67]

Q. Were you asked for your opinion as to how to run the partnership, or how to operate it?

A. No.

Q. Never? A. No.

Q. Did your father ever at any time to your knowledge ask your stepmother for her opinion as to how to operate the partnership?

A. No, sir.

Q. Did he ever at any time ask you for an opinion as to what he should do, policy-wise or how he should manage that partnership?

A. No, sir.

Q. Did you ever hear him ask your brother, Newton Sherry, how or in what way he should proceed in connection with the partnership, Sherry Enterprises? A. No, sir.

Q. Did you ever volunteer at any time that you recollect an endeavor to tell your father how to operate that partnership? A. No, sir.

Q. Did you make any capital contribution yourself? You know what I mean by that, contribution of capital to this alleged partnership?

A. $500.00.

Q. $500.00. Where did you get the $500.00? [68]

A. From my grandmother. It was from my grandmother's estate.

(Testimony of Margaret Ferguson.)

Q. Did you ever actually see the $500.00?

A. Yes.

Q. In what form?

A. It came in a check, in the form of a check.

Q. Made out to you? A. Yes.

Q. And what did you do with the check?

A. I gave it to my father.

Q. Gave it to your father? A. Yes.

Q. What year was that?

A. Gee, Mr. Carr, it was after I came home from the Service, I think. I am not clear on it. It was some time after she died.

Q. That was long after the partnership had been formed, is that right? A. Oh, yes.

Q. And you gave the check, endorsed it over to your father? A. That's right.

Q. Do you know what he did with it?

A. He told me he was going to put it——

Q. I didn't ask you that. I asked you if you knew [69] what he did with it.

A. No.

Q. What did he say he did with it?

A. He said he was going to put it in the business.

Q. Did he say what business?

A. Well, I assumed when he said business——

Q. No, I am not asking you what you assumed. Did he say which business?

A. He said he was going to invest it in the business.

Q. But he didn't say which business?

(Testimony of Margaret Ferguson.)

A. No.

Q. Now, in connection with your brother, of your own knowledge I am asking now, did your brother in any way participate in operating or managing this partnership, Sherry Enterprises, as far as you know? A. No.

Q. What was your brother doing when you came home from the Service?

A. I think he was working at the Bayview Club.

Q. That is the one down in Wilmington?

A. Yes.

Q. Do you know whether or not that was a part of the partnership assets, Sherry Enterprises?

A. No.

The Court: You mean you don't know or that it was [70] not?

The Witness: No, I mean that——

Q. (By Mr. Carr): Do you know?

A. I know that it was a part of the S & P Company.

Q. S & P Company? A. Yes.

Q. How do you know that?

A. I was told all of the businesses were.

Q. When you say all of the businesses, what do you mean?

A. We will get confused, won't we? I mean all of the operating businesses, the bars and restaurants.

Q. Well, now, Mrs. Ferguson, were there some businesses that were not a part of S & P?

(Testimony of Margaret Ferguson.)

A. Not that I know of.

Q. Did you know whether or not Mr. Sherry had partnerships with other people besides Mr. Kalmanovitz? A. Not that I know of.

Q. Did you ever examine the partnership books?

A. No.

Q. Did you ever ask for an accounting of any kind? A. No.

Q. Did you ever receive any of the income from the partnership, Sherry Enterprises?

A. No, sir. [71]

Q. And did you ever yourself pay any taxes for income which you allegedly received from the partnership, Sherry Enterprises?

A. Well,——

Q. Do you understand the question?

A. No, I don't.

Q. Did you ever take any money out of your pocket and pay any taxes on income which you received from Sherry Enterprises? A. No.

Q. Did you ever receive any income from Sherry Enterprises? A. No.

Q. Now, when you returned from the Service, didn't you go to school for a while?

A. Yes, I did.

Q. Where did you go?

A. The University of Southern California.

Mr. Carr: I don't think this has been marked as an exhibit. I will show it to her. You want it introduced, counsel? It is a record out there at school. It is entirely up to you.

(Testimony of Margaret Ferguson.)

Mr. Townsend: I don't particularly.

Q. (By Mr. Carr): Can you refresh your recollection and tell me what [72] date the dates were?

A. The date entered was January 2, 1946—wait a minute, March 7, 1946.

Q. That is the date of entry?

A. That is the date of entry.

Q. When did you terminate?

A. I don't see it here, but I am sure it was in June when the school year was over.

Q. In 1946? A. Yes.

Mr. Carr: No further questions.

I have had it called to my attention that apparently she made an error. I think maybe I better offer this in evidence and ask her to look at it.

Look at the top and see what the date of entry is. If you look at the very top, I think you will find the date.

The Witness: January 2, 1946. Well, there are two different—yes, January 2, 1946.

Q. (By Mr. Carr): Now, have you got it straight?

The Court: You may look at that paper only for the purpose of refreshing your recollection. Your testimony must be based on your recollection and not what you read off the paper.

The Witness: Well, I remember that I went to school [73] as soon as I was able to go to school after I came home. In other words, I came home in November. I couldn't have gone to school in November. It was the middle of the school term. As soon

(Testimony of Margaret Ferguson.)
as I had the opportunity to go, I went and I don't remember the exact date.

Q. (By Mr. Carr): Can you approximate the date? A. I thought it was February.

Q. Of 1946?

The Court: Did you complete a full semester?

The Witness: Yes, I did.

Mr. Carr: I think that is all.

Cross Examination

Q. (By Mr. Townsend): Now, Mrs. Ferguson, directing your attention to Exhibit J which is a donee gift tax return of gifts, I believe you already identified that for Mr. Carr as bearing your signature. Is that correct?

A. Yes, that is correct.

Q. And I believe you stated you were in the Navy at the time you signed this?

A. Well, I have been so confused about dates, if you would tell me the date, I can tell you where I was.

Q. It bears the date of March 15, 1944.

A. Then I would have been in the Navy, yes.

Q. And do you recall receiving this in the mail?

A. No, I don't recall. I am sure I did, but I don't recall.

Q. Do you recall that you were told by letter or otherwise that your father and stepmother were making this gift to you?

A. I would only have been told to sign the papers and return them.

(Testimony of Margaret Ferguson.)

Q. Wouldn't they give some explanation to you?

A. Probably not.

Q. Now, when you got the partnership agreement in the mail didn't the letter that they sent you say something about they were forming a partnership and wanted to take care of you in the future?

A. I honestly can't tell you what the letter said. I have no recollection about it. I am only assuming that a letter came with it.

Q. I see, but you do recall signing that partnership agreement, do you not?

A. Yes, it is my signature.

Q. Did you look at it?

A. Not that I recall.

Q. You don't recall whether you did or did not?

A. That's right.

Q. Well, when did you first become aware, as far as [75] your recollection is concerned, of there being a partnership?

A. I am not sure of the dates. It could possibly have been at some time when I was home from the Navy. Perhaps on a leave that I was told about it.

Q. Directing your attention, Mrs. Ferguson, to Exhibit H which purports to be an agreement amending the original partnership agreement——

Mr. Carr: I have a copy, counsel.

Mr. Townsend: Thank you, that would be very helpful.

Mr. Carr: It is really a duplicate original so if I may, I'd like to have that back.

(Testimony of Margaret Ferguson.)

Mr. Townsend: Surely, I am just going to use it for the witness.

Q. (By Mr. Townsend): This is an agreement purportedly amending the original partnership agreement. This agreement is dated the 1st day of July, 1944, and I believe that bears your signature, does it not?

A. I am not sure that this is my signature. I don't think it is.

Mr. Carr: I didn't hear the answer.

The Witness: I don't think it is. My father had power of attorney. I don't know whether that is my signature or not.

Mr. Townsend: Well, it is in evidence. [76]

Mr. Carr: You have one in evidence already.

Mr. Townsend: Yes.

The Court: The stipulation, I think, states it was signed.

Mr. Carr: That is correct. We thought she did, your Honor. That was our understanding when we stipulated to it, so this comes as a surprise to me, too. I assume all stipulations are subject to the light of truth, so I guess the testimony ought to stand. I submit it should. May I just ask one question, your Honor, of her? Do you mind at this time, counsel?

Mr. Townsend: No, go ahead.

Voir Dire Examination

Q. (By Mr. Carr): Are you in doubt about the signature?

(Testimony of Margaret Ferguson.)

A. I am in doubt about it. I don't know what difference it makes, but it doesn't look like my signature.

Mr. Townsend: I think there are enough other signatures in the records, Mr. Carr.

The Court: It looks similar to the other signatures.

Mr. Carr: It does. We thought it was the same.

The Court: The opening paragraph of the stipulation of facts recites a stipulation that the facts shall be taken as true without prejudice to the right of either party to submit material and competent evidence of any other facts not [77] inconsistent herewith, and I do not believe I will receive any evidence in contradiction to the stipulation.

Mr. Carr: Well, I really don't think it is of great moment, your Honor, in the case. I won't urge the point. This comes as a little bit of a surprise to me. We thought it was settled.

Cross Examination—(Continued)

Q. (By Mr. Townsend): What did you understand when you signed this partnership agreement, Mrs. Ferguson? That would be Exhibit G which was sent to you in the mail with the letter.

A. What did I—I don't understand your question.

Q. What did you understand you were signing when you signed this instrument?

A. I don't recall.

Mr. Carr: Are you talking about the exhibit?

(Testimony of Margaret Ferguson.)

Mr. Townsend: Exhibit G, Mr. Carr.

Mr. Carr: He is talking about Exhibit G.

The Witness: Yes, I understand that. I don't remember what I thought about it. It was a long time ago.

Q. (By Mr. Townsend): And is your testimony the same with respect to your signing the gift tax returns?

A. You mean that I don't remember what I thought about it at the time? [78]

Q. Yes. A. Yes, that's right.

Q. You knew, did you not, that that return would be filed with the government at the time you signed it? A. Yes.

Q. You felt that that was a true statement? Did you have any reason to believe that this was a sham gift or not a true gift?

A. Of course not.

Q. What assets did you contribute to the Sherry Enterprises? A. Of my own?

Q. Yes.

A. The $500.00 that was from my grandmother.

Q. How about the money that was left by your mother, Mrs. Sherry?

A. That was supposed to have been put in as a contribution.

Q. That was your understanding?

A. That was my understanding.

Q. Your father held that money for you?

A. That's right.

Q. You knew it was your money?

(Testimony of Margaret Ferguson.)

A. I knew it had been left for my brother and I.

The Court: How much did that come to? [79]

The Witness: My father told me that it was $20,000.00.

Mr. Carr: Well, I submit, I believe your Honor will point it out, that you aren't going to consider hearsay evidence, and I think all this apparently is hearsay.

Q. (By Mr. Townsend): Your mother also told you, did she not, that she was leaving you $20,000?

A. Yes, she did. She told me that there was that much money that would be ours if anything happened to her.

Q. It was your understanding that that money was contributed to the Sherry Enterprises?

A. That was what I was told, yes.

Q. Now, when you came out of the Navy, that would be in November or earlier than that in 1945—— A. November, 1945.

Q. What did you do exactly?

A. Well, I went to school until the following June.

Q. That was in Los Angeles?

A. University of Southern California.

Q. University of Southern California. Did you work in any way during that period?

A. Not during that period, no.

Q. When did you start working and what did you do, please?

A. Well, I started—I worked for a while in Sherry [80] Dunn, which was a perfume business,

(Testimony of Margaret Ferguson.)

for my father and I don't remember the exact period. It couldn't have been too long, perhaps from September or October. I was married in March. So, there was a period of just a few months.

Q. What did you do for the Sherry Dunn Company?

A. Answered telephones and took messages and things of that kind.

Q. Was it your understanding that Sherry Dunn Company was a part of Sherry Enterprises?

A. Yes, that was my understanding.

Q. You knew that title to real property was being placed in your name during that period, Mrs. Ferguson, did you not? A. Yes, I did.

Q. Was that your own property?

A. No, it was the——

Mr. Carr: Now, I submit that we have no property identified. I don't know whether the witness knows what you are talking about.

Mr. Townsend: Well, she appeared to.

Mr. Carr: Well, I think the property ought to be identified.

Q. (By Mr. Townsend): Well, what property was placed in your name, Mrs. Ferguson?

A. Well, as I recall, there was some lots on Santa [81] Monica Boulevard, and there was a building—no, I don't think that was in my name. I think that was the Marton Holding Company, if I recall correctly.

Q. Mrs. Ferguson, my information is that real estate in the value of $2,500.00 was placed in your

(Testimony of Margaret Ferguson.)

name on June 30, 1946, and that real estate to the value of $52,500.00 was placed in your name on June 30, 1945. That would be the property, I believe, of the Marton Holding Company. Do you recall that?

A. I just stated it. What do you mean, do I recall what? Do I recall what?

Q. Do you recall title to that property being placed in your name?

A. Yes, I just told you that I did.

Q. Now, was that your own property?

A. It was a part of the Sherry Enterprises.

Q. What would you roughly estimate would be the total value of the assets that you owned personally in the years 1945 and 1946?

A. I never considered that I owned any assets personally. They were all a part of the Sherry Enterprises.

Q. Now, did you ever hear of the Marton Holding Company? A. Yes.

Q. What was your connection with that company?

A. Well, there were three partners in it, I think, my brother, and Mr. Rogers, and myself, as I recall. It was a [82] company my father set up. As he told us at the time, he was always worried about protecting our interest and protecting us, and this was the reason that he put this property in our name, or at least that was my understanding at the time it was done.

(Testimony of Margaret Ferguson.)

Q. Did you consider that to be your own property? A. No.

Q. Whose property did you consider it to be?

A. Well, it was a part of the Enterprises. It was really my father's.

Q. During the years 1945 and 1946, as far as your own thinking was concerned, Mrs. Ferguson, did you feel that you were a bonafide member of a partnership, namely, the Sherry Enterprises?

A. At that time I did. Well, I understand the word "partnership" is in contention here, but for all practical purposes, I felt that I was, yes.

The Court: When did your father die?

The Witness: He died the end of May, three years ago.

The Court: Did he still have an interest in Sherry Enterprises at the time of his death?

The Witness: Oh, yes.

The Court: What happened?

The Witness: You mean what happened to the partnership since then?

The Court: Your father's interest in it. [83]

The Witness: Well, there was practically nothing *let* to it at the time he died. I don't quite—there is an estate, so much of this was depleted by the time he died. That is what I am trying to say.

Mr. Carr: May I suggest something, your Honor, that you might ask her what the assets were in the estate. I think the estate is still pending, isn't it?

The Witness: Yes.

Mr. Carr: Tell the Judge.

(Testimony of Margaret Ferguson.)

The Court: I will let counsel bring that out. I am just puzzled by the consequences at his death, whether it was owned one way or whether those interested in it proceeded upon the assumption that it was split four ways, and I think there would be different probate or legal proceedings after his death, depending upon which theory were adopted. I just wondered what, in fact, has happened since his death.

Mr. Carr: I think I can help clarify, if you are in disagreement, you can assert so.

The Court: I don't want to interrupt Mr. Townsend.

Mr. Townsend: It is all right.

Mr. Carr: As far as I know, of course I don't represent the estate. The estate—I did represent Mr. Sherry and his wife in the tax proceedings, but another lawyer intervened and after Mr. Sherry's death, she withdrew and went on her own and went by default in the tax proceedings in other [84] cases, so there was a default and no petition was filed, but in the meantime, I am told that the estate turned out to have nothing in it, that it was defunct.

Mr. Townsend: That is my understanding.

Mr. Carr: That it had been dissipated or something had happened to it prior to his death.

The Court: That Sherry Enterprises had no value at that time?

Mr. Townsend: The estate had no value, at least

(Testimony of Margaret Ferguson.)
listed in the name of the estate, had no assets listed in the estate.

The Court: Even on the government's theory, Mr. Sherry would have had a quarter interest in Sherry Enterprises and on the petitioner's theory, he would have had a complete interest in it. My question is what happened to Sherry Enterprises?

Mr. Townsend: That is the tax proceeding that Mr. Carr was talking about where a 90-day letter was sent to Mr. Sherry based on the theory that he was a 25 percent partner, and he defaulted.

Mr. Carr: The deceased's estate defaulted, and the wife also defaulted, I understand. I represented her, but she didn't see fit to have me file a petition.

The Court: Was it on the theory that he had a quarter interest? [85]

Mr. Townsend: A quarter interest, your Honor.

The Court: Did the government take any position at all to protect itself in the event that it were wrong in its theory in this case?

Mr. Townsend: It did not.

The Court: It didn't seek to collect or to propose a deficiency based on the theory that he owned it all?

Mr. Townsend: No, it did not.

Mr. Carr: Well, from a practical standpoint, it turns out the same. We are fighting over a dead turnip, your Honor. That is what it amounts to.

Q. (By Mr. Townsend): Now, Mrs. Ferguson, you had some relation with the Marguery Corporation, did you not? A. Yes.

(Testimony of Margaret Ferguson.)

Q. What was your connection with that?

A. It was—I was at one time the president of the corporation.

Q. You were also a stockholder in that corporation? A. That's right.

Q. Are you still today? A. Yes, I am.

Q. Are you still president of that corporation today? A. No, I am not.

Q. But you are still a stockholder? [86]

A. That's right.

Q. How did you acquire your stock in that corporation?

A. Well, it was given to me by my father.

Q. When? A. 1947.

Q. In 1947? A. Yes.

Q. Is that the corporation that ran Lucy's Restaurant? A. Still does, yes.

Q. And you have worked also at Lucy's Restaurant, did you not? A. I still do.

Q. You still work there at Lucy's?

A. Yes.

Q. And what is your position at Lucy's today?

A. Well, I am managing the restaurant today.

Q. You are managing it?

A. That's right.

Q. And Lucy's is owned by the Marguery Corporation? A. That is right.

Q. And you acquired your stock in Marguery Corporation from your father back in 1947?

A. That is right.

(Testimony of Margaret Ferguson.)

Q. Did you consider that stock to be your own stock at the time it was given to you? [87]

A. Yes.

Q. You did not consider it to be a part of Sherry Enterprises?

A. No, I considered—I really considered it to be my stock.

Q. To be your own stock? A. Yes.

The Court: Where did it come from?

The Witness: My father.

The Court: Well, did you know whether or not it had been a part of Sherry Enterprises at any time?

The Witness: No.

The Court: You mean you don't know, or you know it was not?

The Witness: Well, if I recall correctly, I got the stock at the time that he bought the restaurant. The stock that—yes, that's right.

The Court: You got it at the time you bought it?

The Witness: Yes.

Q. (By Mr. Townsend): Do you know that he used funds of Sherry Enterprises in order to buy it? A. Yes, I think he did.

Q. Now, Mrs. Ferguson, you are presently the owner of a fourplex apartment house at 647 North Irving Boulevard, [88] Los Angeles, are you not?

A. That is right.

Q. How did you acquire that property?

A. From my father.

Q. When?

(Testimony of Margaret Ferguson.)

A. I don't remember exactly. It was several years ago.

Q. Was that property also held for Sherry Enterprises before it was turned over to you?

A. I can't tell you that. I don't recall.

Q. Did you consider yourself the owner of that property at the time you received it, or did you consider that you held it for Sherry Enterprises?

A. Well, I consider myself the owner.

The Court: Did you file any donee gift tax return to show that it was given?

The Witness: Did I?

The Court: Yes.

The Witness: No.

Q. (By Mr. Townsend): What funds were used to acquire that apartment house?

A. I don't know.

Q. You don't know? A. No.

Q. Do you know whether or not it was Sherry Enterprises' funds? [89]

A. No, I don't. It was a very complicated transaction as I recall, and I am not sure where the funds came from to buy it.

Q. Do you recall anything about a transfer of lots back and forth to acquire that property?

A. No.

Q. La Cienega lots?

A. No, to buy that property? No.

Q. What other property do you own today which you acquired from your father or from the Sherry Enterprises?

(Testimony of Margaret Ferguson.)

A. I have a house at 1810 Courtney Avenue which was bought—was a part of the Sherry Enterprises.

Q. When did you acquire that property?

A. 1950.

Q. In 1950? A. Yes.

Q. And title is in your name?

A. That's right.

Q. Do you consider that to be your own property?

A. Well, let me state it this way. I do. I have made the mortgage payments on it, and I am still making the mortgage payments on it.

Q. But at one time it was an asset of Sherry Enterprises? A. That's right.

Q. What would you say the approximate value of that [90] home would be?

A. Oh, probably $35,000.00. It is a triplex. It is not just a home.

Q. I see, but that is in addition to the other apartment house we are talking about?

A. Yes.

Q. What would you say the approximate value of that fourplex apartment house on Irving Boulevard is?

A. It is a very old building, maybe $14,000.00, something like that.

Q. What would you say approximately is the value of the stock in Marguery Corporation which you hold?

A. It is not worth a thing.

(Testimony of Margaret Ferguson.)

Mr. Carr: Talk louder, we can't hear you.

The Witness: I don't think it is worth anything, Mr. Carr. It is a very shaky business.

Q. (By Mr. Townsend): You do not think that Lucy's Restaurant is worth anything?

A. Well, let me say that we haven't been able to sell it for anything.

Q. But it is presently operating as a business?

A. That's right.

Q. Now, are there any other assets besides that you have acquired from your father or from Sherry Enterprises? [91] A. No.

Q. How about lots on La Cienega? Didn't you at one time hold some lots on La Cienega?

A. I never recall holding—my father had lots on La Cienega, but not me. They were in my father's name as I recall.

Q. Mrs. Ferguson, I show you what has been marked for identification as Respondent's Exhibit L which purports to be a waiver of restrictions on the assessment and collection of deficiency income tax. In other words, you are agreeing to an additional deficiency of $1109.75. Attached thereto is a revenue agent's report which was sent to you at 5444 Melrose Avenue. The date is September 9, 1948, and this additional assessment is purportedly to increasing your distribution of share of income from the Sherry Enterprises as partnership. Is that your signature thereon? A. Yes.

Q. Do you recall signing that?

A. No—when was this sent? When was this——

(Testimony of Margaret Ferguson.)

Q. The next page will show you an address.

A. I lived out of the city for a while after I was married. No, I think I was home at this time, but I don't recall signing this.

Q. You don't recall anything about it?

A. No. [92]

Q. Would you look through it and see if you can recall anything about it, Mrs. Ferguson?

A. No, all of these things were presented to me to sign, and I never knew. I took them to be correct and I signed them.

Q. Did you realize when you signed that that you were agreeing to a tax of $1100.00?

A. Probably not.

Q. Now, Mrs. Ferguson, I believe Mr. Carr asked you this, but I wanted to ask you again.

Were there ever business meetings between the four members of the family, and on this purported partnership which you attended? It wouldn't have to be a formal meeting.

A. There were discussions at different times, and very few, maybe two or three where all the members of the family would be present. This would be at a social gathering where this discussion might come up. There were never any formal meetings or you know, calls to discuss business, that sort of thing.

Q. Did you ever discuss the acquisition of new businesses or how business was going on or things like that at these meetings?

A. Mostly they were meetings, and my father

(Testimony of Margaret Ferguson.)

would say I bought or sold, and we'd sit there and shake our heads, and that was about the extent of it.

Q. Sounds like something my family would do, also. [93] You spoke about your brother, Newton, working for Bayview——

A. I think it was the Bayview Club, if I am not mistaken. I know Bayview was in the name.

Q. And who did you understand he was actually working for then?

A. He was working for the S & P Company. At least, that was my understanding.

Q. Which, in turn, you understood to be an asset of the Sherry Enterprises?

A. Half of it.

Q. Half of it? A. Yes.

The Clerk: M for identification.

Mr. Carr: That is a copy of the statement? We have a copy of it.

(The document above-referred to was marked Respondent's Exhibit M for identification.)

Q. (By Mr. Townsend): Now, Mrs. Ferguson, I show you what has been marked for identification as Respondent's Exhibit M and which purports to be the voluntary sworn statement of Mrs. Margaret Ferguson given to the Office of the Intelligence Unit, Bureau of Internal Revenue in this building on May 15, 1950.

A. I remember it well.

Q. You remember that? [94] A. Yes.

Q. Do you recall or can you tell me if that is

(Testimony of Margaret Ferguson.)

your signature thereon? A. Yes, it is.

Q. And would you read that paragraph just above your signature, please? Would you read it aloud, please?

A. "I have carefully read the foregoing transcript of my statement, Pages 1 to 30, and I hereby certify to the best of my knowledge and belief it is a true and correct transcript of my answers to the questions therein propounded."

Q. Would you just glance through each page, Mrs. Ferguson, and see if each page bears your initials?

Mr. Carr: I think that we will stipulate that it does, counsel. I am sure it is the same statement I am talking about. Is this the one?

Mr. Townsend: Yes, it is.

Mr. Carr: Well, we won't require you to prove it.

Mr. Townsend: Respondent offers in evidence the document just identified by this witness.

Mr. Carr: Objected to on the ground it is not proper impeachment. It is hearsay. No proper foundation has been laid. It has no evidentiary value whatsoever. The only purpose for which it can be used is to impeach.

Mr. Townsend: Your Honor, it is offered as admissions of this witness. [95]

The Court: Overruled. It will be admitted.

The Clerk: M.

(The document heretofore marked Respondent's Exhibit M was received in evidence.)

Mr. Townsend: No further questions.

(Testimony of Margaret Ferguson.)

Mr. Carr: May I ask a few more?

Redirect Examination

Q. (By Mr. Carr): Mrs. Ferguson, you say you felt in answer to counsel that there was a partnership. Will you be more explicit? What do you mean by "you felt there was a partnership"?

A. My father told me there was a partnership.

Q. Well, is that the extent of what you based your conclusion on, the fact that he told you there was a partnership? A. Yes.

Q. Now, you say that you are a stockholder in the Marguery Corporation and that was given to you in 1947. What percent of the stock?

A. I don't recall.

Q. What percent do you actually have now?

A. Twenty.

Q. Was that what was given to you?

A. No. No, there were changes made in the stock, Mr. Carr, from the time it was given until the present time. [96]

Q. Well, at the present time you hold 20 percent in the stock? A. That's right.

Q. Now, the corporation, does it own the building? A. No.

Q. Has a lease? A. That's right.

Q. How long a lease?

A. Well, there is an option that expires May 1st and——

Q. What year?

A. This year. This May 1st.

(Testimony of Margaret Ferguson.)

Q. And are you making—have you any net profits there now? A. No.

Q. Is the business winning or losing?

A. Well, it is barely breaking even.

Q. And when you say that the stock that you own is worth nothing, do you actually mean that?

A. Yes, I actually mean that.

Q. Have you tried to sell it?

A. We have even tried to sell the business, let alone the stock, and haven't been successful.

Q. Now, this property, 647 North Irving Boulevard, that was in the name of someone else for some period of time, wasn't it? [97] A. Yes.

Q. Who? A. Albert Levine.

Q. And who is Albert Levine?

A. He was an attorney for my father.

Q. And do you recollect how that property was gotten out of his name?

A. By lawsuit, I recall.

Q. By whom? A. By you.

Q. Well, I mean who was the party plaintiff, do you remember?

A. By me, you mean—oh, excuse me, yes.

Q. And you recollect that we filed a suit in the Federal Court and finally got the property back?

A. That's right.

Q. Now, then, you might also tell the Court that I have a lien on that property. We don't want to keep anything from the Court.

A. That is right.

Q. Is that correct? A. Yes.

(Testimony of Margaret Ferguson.)

Q. In writing? A. Yes.

Q. And have had since before you got it in your name, [98] is that correct?

A. That is right.

Q. At the time it was in Mr. Levine's name, I took a written assignment of that property from yourself, your mother, your father and your brother, is that correct?

A. That is correct.

Q. And still have it as of record?

A. That's right.

Q. So, you have no hopes of ever getting that property back, do you? A. No.

Q. Now, the property, the 1810 Courtney Avenue—incidentally, you might tell the Court who defended your father in the criminal tax case.

A. You did.

Q. And I take it I have represented you and your brother and your family until your mother pulled out over the years since that time. You remember when the criminal trial was?

A. About five years, in August, as I recall.

Q. 1952, wasn't it? This property on Courtney Avenue, you say, that is a triplex?

A. That's right.

Q. Who lives there?

A. My stepmother lives in one unit and I live in one, and we rent the third. [99]

Q. Incidentally, have you ever received anything from the probate of the estate?

A. No.

(Testimony of Margaret Ferguson.)

Q. Has anyone in the family; your stepmother, your brother, or yourself? A. No.

Q. To your knowledge, were there any assets in the estate? A. No.

Q. Do you know what happened to the assets of the partnership, Sherry Enterprises?

A. No. I didn't know there were any. This is a very confused——

Q. You knew, Mrs. Ferguson, that the partnership owned or had leases on various restaurants here in town at one time, is that right?

A. Sherry Enterprises?

Q. Yes, through S & P Company?

A. Oh, yes.

Q. Do you know what happened to those enterprises? A. No.

Q. Are they still in business?

A. The restaurants and bars and things like that?

Q. Yes.

A. Yes, I don't know what happened to them.

Q. Do you have anything to do with them?

A. No.

Q. Well, what happened to them, if you know?

A. Well, I remember—when Mr. Kalmanovitz and Mr. Sherry split their partnership, I think that they were all gone and we didn't have anything after that. As I recall, Mr. Kalmanovitz——

Q. I will read the list off the income tax returns. I am referring now to Exhibit I which is the gift tax return of Nathan Sherry, and he lists the fol-

(Testimony of Margaret Ferguson.)

lowing: He says, "In each of the two above named donees I have transferred an interest in the properties herein described and in the properties and values specified. Date of all gifts." Now, Item 1—6.25 interest in S & P Company, a co-partnership, what happened to the S & P Company?

A. It has been dissolved.

Q. Jerry's Joint, 211 Ferguson Alley, what happened to it, do you know?

A. Yes, the city tore it down.

Q. Well, did you get any money from it?

A. No.

Q. Who got the money?

A. I don't know.

Q. Hatfield's Cafe at 8108 South Central Avenue. What happened to that? [101]

A. I don't know.

Q. Did you get any money from it?

A. No.

Q. Hatfield's Cafe, 9301 South Vermont, what happened to that? A. I don't know.

Q. Royal Cafe at 10425 South Vermont Avenue in Los Angeles. Who got that? Do you know who owns that? A. No.

Q. Now, despite my eyes, I see it is the Pigpen Cafe. Do you know what happened to that?

A. No.

Q. Do you know who owns it? A. No.

Q. Did you get any money out of it?

A. No.

Q. Then, the Hollywood Recreation Center at

(Testimony of Margaret Ferguson.)

1513 North Vine Street. Do you have any interest in that? A. No.

Q. Do you know who owns it? A. No.

Q. Do you know what happened to it?

A. No.

Q. The Keith Jones at 727 South Hill Street. Do you own that? [102] A. No.

Q. Do you know who does own it?

A. No.

Q. What happened to it?

A. I don't know.

Q. The Jade Cafe at 6619 Hollywood Boulevard, what happened to that? A. I don't know.

Q. Did you ever have any interest in it that you know of? A. No.

Q. Did you ever receive any income from it?

A. No.

Q. The Stardust Cafe at 6645 Hollywood Boulevard, what happened to that?

A. I don't know.

Q. You don't know who owns it or what happened to it? A. No.

Q. And the Monticello Cafe, did you ever hear of that? A. Yes, I heard of it.

Q. What happened to it?

A. I don't know.

Q. Did you get anything out of it?

A. No.

Q. Do you know who owns it now?

A. No. [103]

(Testimony of Margaret Ferguson.)

Q. And the Pago Cafe at 5813 York Boulevard, who got that? A. I don't know.

Q. Did you get anything out of it?

A. No.

Q. Do you know who owns it now?

A. No.

Q. Jerry's Joint on Wilshire Boulevard, what happened to that? A. I don't know.

Q. Do you know who owns it? A. No.

Q. And now a night club called the Swing Club, do you know anything about that? A. No.

Q. Did you ever hear of that club?

A. No, I never heard of the Swing Club.

Q. Did you know whether it was a partnership asset or not? A. No.

Q. Can you tell me now what the partnership assets were of Sherry Enterprises in 1945?

A. No.

Q. The properties? A. No. [104]

Q. Can you name any of them?

A. In 1945? No.

Q. Well, did he have Lucy's at that time, do you know? A. No.

Q. And as far as you know, then, as I understand it, you don't know what properties were owned by Sherry Enterprises in the calendar year 1945? A. That is right.

Q. How about the year 1944? A. No.

Q. When did you first learn something about the properties that were owned by Sherry Enterprises, approximately?

(Testimony of Margaret Ferguson.)

A. The first thing I ever knew about it was when he bought the building in Pasadena, as I recall.

Q. Now, then, one or two other questions and then I am finished.

The $20,000.00 that you said you understood came from your mother's estate, you never saw the twenty thousand, did you? A. No.

Q. Did you ever see any kind of paper to show a deposit for the $20,000.00?

A. I was only 14 years old, Mr. Carr.

Q. And who told you there was $20,000.00?

A. My father. [105]

Q. Do you remember where he told you that?

A. No.

Q. Do you know where the estate was probated?

A. No.

Q. And do you know in what form it was put into this partnership? A. No.

Q. Where was it kept through those years until the time it was put in the partnership, if you know? A. I don't know.

Q. Were you told where it was kept?

A. No.

Q. Did you know of any bank account where this twenty thousand was kept? A. No.

Q. What year would you say it was that your grandmother passed on and left this $20,000.00?

The Court: It was her mother, was it not?

Q. (By Mr. Carr): I mean your mother.

(Testimony of Margaret Ferguson.)

A. My mother died February 1st, 1947—excuse me, 1937.

Q. The partnership was formed, as you know, in 1943, that is, the papers were executed. Now, during those years, you don't know where the twenty thousand was kept?

A. No, sir. [106]

Q. Mr. Sherry never told you that?

A. No.

Q. How old are you now?

A. Thirty-four.

Q. And when you signed this partnership agreement in 1943, how old were you?

A. I must have been 20 or 21.

Q. Well, how old were you?

A. Well, when in 1943.

Q. What is your birthday?

A. November 28th.

Q. You signed this partnership——

A. I was 20.

Q. Going on 21? A. Yes, that's right.

Q. Did you and your brother ever sit down and discuss why you weren't getting anything out of this partnership? A. No.

Q. Did you ever ask your father why you were not receiving anything out of this partnership?

A. No.

Q. Did you ever ask your stepmother why you weren't getting something out of the partnership?

A. No.

Q. Did you ever hear your stepmother try to

(Testimony of Margaret Ferguson.)

tell your [107] father what to do in this partnership? A. No.

Q. Were you ever around when she attempted to ask questions about it?

A. No, she never did, not to my knowledge.

Q. Did she ever come over to Lucy's?

A. Oh, yes, to eat, you mean?

Q. Well, I mean for business purposes?

A. Oh, no.

Q. What purposes did she come over there?

A. Social.

Q. What do you mean by "social"?

A. To eat.

Mr. Carr: No further questions.

Recross Examination

Q. (By Mr. Townsend): Mrs. Ferguson, you know that the S & P Company was originally a partnership between your father and Mr. Kalmanovitz, is that correct?

A. That is correct.

Q. And you know that that was later changed into a corporation, don't you, or purported——

A. To tell the truth, I heard it for the first time here today.

Q. You knew that your father and Mr. Kalmanovitz were [108] having some business difculties? A. Yes.

Q. And you know that they decided to sever their business relationships? A. Yes.

Q. And you know that your father got out of

(Testimony of Margaret Ferguson.)

S & P Company and got something for his interest, didn't he? A. Yes.

Q. So, in other words, your father turned over all these clubs that we were talking about to Mr. Kalmanovitz and in return for that your father got the Clover Club and lots on La Cienega Boulevard. You know that?

A. Yes, that's right.

Q. What happened to those lots and what happened to the Clover Club?

A. The Clover Club burned down, and the lots he sold.

Q. And how about the lot that the—or the property that the Clover Club was on?

A. I think he sold them. He must have because we don't have them.

Q. Now, directing your attention to Exhibits A and B which are copies of your income tax returns, are they in front of you? A. Yes.

Q. You recall signing those returns, don't you?

A. My signature is on them. I don't recall signing them.

Q. One was signed on March 13, 1946, and the other one was signed some time in—in—apparently prior to March 15th of '47, right around that period? A. Yes.

Q. Now, those returns show that you had a net income for the year 1945 of some $21,949.00. For the year 1946 they show that you reported a net income of $19,156.85. Is it your testimony that you never even looked at those figures, that you didn't

(Testimony of Margaret Ferguson.)

know what you were doing when you signed these returns?

A. I didn't say I didn't look at the figures. Undoubtedly I did look at the figures. They had no meaning to me.

Q. Weren't you curious as to how you were reporting an income of nineteen thousand, and twenty-one thousand?

A. No, I assumed that this was income that had to do with my father's business, and that these returns were correct.

Q. In other words, when you filed these returns you felt that you were a partner and you were reporting your right share to the partnership income?

A. When I signed these returns, I thought that my father had prepared them, that they were correct and I would sign them. I don't know that I had any feelings about being [110] anything.

Q. Well, did you consider that this so-called "partnership" was a tax avoidance scheme that you were entering into with your father, your stepmother and your brother so that your father would be able to save Federal income taxes?

A. You want to know what I thought? My father and stepmother didn't get along very well. I was told that this partnership was set up to protect us in case of my father's death. That was the only reason completely.

The Court: By protection, you mean in the event

(Testimony of Margaret Ferguson.)

of your father's death you would have a certain percentage of this property? It would be yours?

The Witness: That's right.

Q. (By Mr. Townsend): Now, was there any conversation at any time with your father or any of the other members of the family that would indicate that this partnership agreement was a sham and was unreal? A. No.

Q. So far as you were concerned, when you went into this partnership you considered it a bonafide, genuine partnership?

A. For as much as I knew of it at the time, yes. I mean yes, that's right.

Q. And you felt when you executed these documents that [111] you were entering into a genuine partnership as far as you were concerned?

A. A family partnership, yes.

Q. Now, we discussed Lucy's Restaurant very briefly. Doesn't Lucy's Restaurant have certain substantial assets itself?

A. I wish you could find them.

Q. Don't they——

A. We have two liquor licenses, yes.

Q. Do they own the building, or is it leased?

A. No, the building is leased.

Q. And they have equipment in the building?

A. Very antiquated.

Q. How large a restaurant is it?

A. It is quite a large restaurant. It seats about 300 people.

Mr. Townsend: I have no further questions.

(Testimony of Margaret Ferguson.)

Redirect Examination

Q. (By Mr. Carr): Oh, yes, I wanted to ask the one question. Counsel asked you about the sale of some lots and about the money from the Clover Club. Did you get any of the money?

A. No.

Q. Did your brother get any that you know of?

A. No.

Q. You don't know what happened to the money? [112] A. No.

Mr. Carr: That is all.

Mr. Townsend: That is all.

Mr. Carr: Mr. Kalmanovitz.

Whereupon,

PAUL KALMANOVITZ

called as a witness by and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

Direct Examination

Q. (By Mr. Carr): Will you please state and spell your name?

A. Paul Kalmanovitz, K-a-l-m-a-n-o-v-i-t-z.

The Clerk:——m-a-n-o——

The Witness: ——v-i-t-z.

Q. (By Mr. Carr): Your address?

A. 15001 Vanowen, Tarzana.

Q. You go under the name Mr. Paul now, don't you? A. Short.

Q. I don't mean any implication, but that is the name you use? A. That is right.

(Testimony of Paul Kalmanovitz.)

Q. You were at one time a partner with a man by the name of Nathan Sherry? [113]

A. I was.

Q. When did it begin?

A. Originally was Olympic Corporation, Nathan Sherry in December, 1940. Subsequent——

Q. Did you develop then into a partnership called S & P? A. That is correct.

Q. About when did that partnership start, Mr. Paul?

A. Oh, early part in the '40's, '41 or '42.

Q. And who were the partners?

A. Nathan Sherry and myself.

Q. And did you ever hear of a partnership being formed by the name of Sherry Enterprises?

A. During the trial, 1951 or so.

Q. Prior to that time, prior to the trial, you are referring now to the criminal trial of Mr. Sherry?

A. That is right.

Q. Prior to that time did you ever hear of the partnership Sherry Enterprises?

A. I think I have slight recollection. Mr. Hughes told me once.

Q. Do you remember about when that was?

A. '47, '48.

Q. Now, can you very quickly tell me to the best of your recollection, I realize you may not remember them all, [114] give me the names of the cafes or properties that were in the S & P Company in 1944 and '45? A. Oh, yes.

Q. Give them to us, will you, please?

(Testimony of Paul Kalmanovitz.)

A. We had Jerry's Joint downtown, Keith Jones, Pago, Monticello, Hollywood Recreation, Jade, Stardust, Clover Club, Monticello, Pigpen, Hatfield, 8001 South Central, Five and Ten. We had some in San Francisco, in Oakland, and Lake Shore Lounge, and some in Pasadena for a while.

Q. Now, were they owned by the S & P Company, a partnership? A. Yes.

Q. And who were the partners at that time?

A. Nathan Sherry, and myself, with the exception for a while we had other partners, three Lyon Brothers. We had a partner out in San Francisco, gentleman named Marquette, and Lou Rab.

Q. To your knowledge, were the two children of Sherry participating in any way in the operation of those businesses, any of them that you have named during the years '44 or '45?

A. With one exception, I believe Sherry Junior was working for a time being as a bartender in Bayview for a few months.

Q. You mean Newton Sherry?

A. Newton Sherry was employed when he came back from [115] the Service for a few months as a bartender in Bayview.

Q. Were you ever notified that the Sherry Enterprises owned any part of S & P Company?

A. No.

Q. Did anyone ever sit down in a meeting and represent Sherry Enterprises when you were discussing partnership matters?

(Testimony of Paul Kalmanovitz.)

A. Not whatsoever. He had an attorney for a while from Baltimore.

Q. Levin, L-e-v-i-n? A. Some name.

Q. Did he ever attempt to discuss the rights of Sherry Enterprises in connection with running those businesses?

A. No, that was in conjunction with liquidation.

Q. When did you end your affairs with Mr. Sherry? A. 1947.

Q. And up to that time did anyone ever sit down with you and attempt to represent Sherry Enterprises in connection with these businesses you have enumerated? A. None whatsoever.

Q. Then, do I understand, that the first time you heard it definitely said about Sherry Enterprises owning a part of this S & P partnership was at the criminal trial in 1952?

A. No, counsel, I believe Don Hughes mentioned to me years back, I mean, I have slight recollection on that subject.

Q. By the way, what participation did Mr. Sherry have [116] in actually managing these concerns that you have enumerated?

A. Oh, to a slight degree.

Q. Who actually did the managing?

A. I was the managing partner.

Q. Where was the main office?

A. 1539 North Vine Street.

Q. Did either Mr. Newton Sherry or Miss Margaret Sherry ever have an office or desk in that place? A. No.

(Testimony of Paul Kalmanovitz.)

Q. Did you ever see them in that place at any time?

A. Oh, most likely seen them in three, four years, a couple of times. Miss Sherry.

Q. Do you ever remember seeing Mr. Newton Sherry in that office?

A. Occasionally he would come in and see his father, rare occasions.

Q. Did he ever at any time ask to see the books of the S & P partnership to your knowledge?

A. No.

Q. Did he ever make any demands upon S & P for an accounting of any kind?

A. None whatsoever to my knowledge.

Q. Did Mrs. Ferguson, formerly Miss Sherry, ever make those demands?

A. Not to my knowledge. [117]

Q. And when you severed—terminated the partnership rather, that was in '47? A. '47.

Q. And did Mr. Newton Sherry at that time have anything to do with the termination of that partnership?

A. No, it was Mr. Sherry and his attorneys.

Q. Which Sherry? A. Senior.

Q. Nathan Sherry? A. That is correct.

Q. Did Mrs. Margaret Ferguson attend or have anything to do with that termination?

A. No.

Q. And the funds that were received, were there any funds received by the way, when you separated?

(Testimony of Paul Kalmanovitz.)

A. No. He received seven lots free and clear, and the Clover Club property free and clear.

Q. Who received it? A. Mr. Sherry.

Q. And were the deeds made out to your knowledge to whom?

A. That I don't remember. The attorneys prepared the papers.

Q. Were you in the negotiations?

A. I was. [118]

Q. And who did you negotiate with?

A. Mr. Sherry and his attorneys.

Q. And did ever one of these children attend one of the negotiations? A. No.

Q. And the settlement was that you would receive everything in the partnership, and in turn give to Mr. Nathan Sherry what now specifically?

A. Seven lots on La Cienega, and the Clover Club property; personal, building and real property.

Q. Is that all? A. That is all.

Q. Was Lucy's or Marguery Corporation ever an asset of the Sherry Enterprises?

A. Was not.

Q. Let me get that address—are you acquainted with the property at 1810 Courtney?

A. Don't even know where it is.

Q. Was that ever at any time an asset of S & P?

A. No.

Q. Never heard of it before? A. No.

Q. How about 647 North Irving Boulevard, was that ever an asset of S & P? A. Never. [119]

(Testimony of Paul Kalmanovitz.)

Q. Ever heard of it before?

A. Never did.

Mr. Carr: That is all.

Cross Examination

Q. (By Mr. Townsend): Did you ever hear of the Hollywood Recreation Company, Mr. Kalmanovitz? A. Oh, yes.

Q. Did you own a part of that?

A. Yes, the Hollywood Recreation was consisting of Nathan Sherry, myself and three Lyon Brothers. Originally was corporation or partnership. I don't know which one came first.

Q. How about Brooks Cafe?

A. Brooks Cafe, yes, that was on Sixth Street. That was Irving Fidler, Nathan Sherry and myself.

Q. How about the Silver Dollar Cafe?

A. That is in Pasadena. Originally belonged to Hollywood Recreation, and then subsequently S & P Company. Then, we sold it to Carl Smith.

Q. What year was that?

A. We acquired in 1933 or '34. I don't recall exactly. We had it a couple of years only, two or three years.

Q. To your knowledge, did Mr. Sherry keep on with the Silver Dollar Cafe? After you got out?

A. No, we got out together. Was awfully complicated operation and we sold it to Carl Smith. He passed away subsequent—got out at the same time.

Q. Now, Mr. Sherry attended considerable meetings of the S & P Company?

(Testimony of Paul Kalmanovitz.)

A. Oh, yes, he was there every day.

Q. Would you say that he represented his interests adequately?

A. Well, Mr. Sherry used to come down late in the afternoon. He stayed late at night and talked to customers and what have you. I did all the managing of it.

Q. You did the managing?

A. That is correct.

Q. And I believe you and Mr. Nathan Sherry had a falling out?

A. We had a disagreement of policies.

Q. I see, and you determined to break off relationships? A. That is correct.

Mr. Townsend: I have no further questions.

Mr. Carr: Thank you. May he be excused, your Honor?

The Court: Yes.

(Witness excused.)

Mr. Carr: I have one more witness, your Honor, be very brief, Mr. Murphy.

(Short recess taken.) [121]

Whereupon,

JAMES F. MURRAY

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your name and address for the record, please?

The Witness: James F. Murray, 126 Catherine Park Drive, Glendora.

Direct Examination

Q. (By Mr. Carr): What is your occupation?

A. I am an accountant.

Q. Were you acquainted with Mr. Nathan Sherry prior to his decease? A. I was.

Q. Were you associated with him in any way, Mr. Murray?

A. I was associated with him up to September 30, 1943, and from around March 15, 1949, as far as doing any accounting work.

Q. Did you make out the returns—were you acquainted with the partnership—I keep saying "partnership." I assume the record will assume that I understand alleged partnership, with the partnership called Sherry Enterprises?

A. Was I acquainted with it? [122]

Q. Yes.

A. I knew that there was a so-called "partnership" formed. It was going to be formed, and it was going to be formed around October 1st, 1943, and at that time I was keeping the books for the Monticello Cafe, and the Hollywood Cafe. I turned them over to Hughes & Yessner in Hollywood.

(Testimony of James F. Murray.)

Q. Did you make out any returns for Sherry Enterprises, income tax returns?

A. Not during the period under question.

Q. When was the first time you made out a return? A. In 1947.

Q. For what year was that?

A. That would have been for the year from July 1st, 1946 until June 30, 1947, I think.

Q. And did you make out any individual returns for Margaret Lillian Sherry?

A. I made the returns out after—in March of '47 for the year '46 off a partnership return that was prepared by Yessner & Hughes in Hollywood.

Q. I will show you here Exhibit B which purports to be—which is the copy of the individual return of Margaret Sherry for the year 1946. Is that right? A. That is correct.

Q. Did you prepare that?

A. I prepared that off the partnership return that was [123] prepared by Yessner & Hughes.

Q. Who requested you to prepare that return?

A. At the time these books were turned over—these tax returns were turned over to me by Mr. Hughes without me being asked anything at all, and I, in turn, prepared the returns off of those tax returns in the file.

Q. What I am getting at, did Mrs. Ferguson, then Miss Margaret Sherry, did she request you to make up that return?

A. Not to my knowledge. They would have been

(Testimony of James F. Murray.)

made up on the request of Mr. Sherry if anyone requested, or Mr. Hughes.

Q. By the way, during 1945 where did you have an office?

A. I think at 606 South Vermont.

Q. And did Mr.—was Mr. Sherry in Lucy's at that time?

A. No, Lucy's wasn't bought until July 1st, 1947.

Q. And where did Mr. Sherry have his office in 1945, if you recollect?

A. Mr. Sherry's office, if you could call it an office, was with the S & P Company on Vine Street.

Q. Were you here when Mr. Kalmanovitz was testifying? A. Yes.

Q. Is that the place?

A. That is the place.

Q. Now, what did you do with this 1946 return, Exhibit B, after you prepared it, do you remember?

A. After that return was prepared, it was probably sent [124] over—that return was taken out to Elm Drive to be signed and the check to be picked up on it.

Q. Do you know who picked the check up?

A. I couldn't honestly say, Mr. Carr. Maybe someone from my office picked it up, one of my employees.

Q. Do you know who issued the checks?

A. Mr. Sherry.

Q. Which Mr. Sherry?

A. Mr. Nathan Sherry probably decided——

(Testimony of James F. Murray.)

The Court: You say he probably did issue them or he did issue them?

The Witness: They did. I probably got the checks from Mr. Sherry because I wouldn't have gotten them from Miss Sherry or Mr. Newton Sherry. I would have got no checks from either one of those two. I never have gotten any checks from those in payment of any taxes.

Q. (By Mr. Carr): Now, then, I will show you Exhibit D which is a return for 1946 of Mr. Newton Ivan and Lois Sherry. Did you prepare that?

A. Yes, we did. That was prepared by our office.

Q. When you say "we" you mean who?

A. I prepared these returns.

Q. Who requested you to prepare that return?

A. Mr. Sherry requested me. [125]

Q. Which Mr. Sherry?

A. Mr. Nathan Sherry, deceased, requested me to prepare these returns.

Q. When you had finished the preparation what, if anything, did you do with that return?

A. This return, Sherry was living at Elm Drive at that time.

Q. When you say "Sherry," I have to know which one.

A. Mr. Nathan Sherry was living at Elm Drive at that time, and I assume we went out to Elm Drive, had these signed and the checks were picked up.

Q. Do you have any recollection of it?

(Testimony of James F. Murray.)

A. I couldn't—I can say that we went out there. We had the returns signed and the checks picked up, Mr. Carr.

Q. Who signed the return, do you know?

The Court: You are speaking now with respect to Mr. Newton Sherry?

The Witness: Mr. Newton Ivan Sherry signed this return and Margaret Lillian Sherry signed this return.

Q. (By Mr. Carr): I am speaking now with respect—let's stay on the one. Let's stay on Exhibit D. Is that the one of Newton?

A. That is Newton Ivan Sherry, and Lois Sherry.

Q. Do you know who issued the check to pay the tax for that return? [126]

A. Those checks were issued by Mr. Sherry.

Q. Which Sherry?

A. Mr. Nathan Sherry.

Q. Were you ever consulted at any time by Mr. Newton Sherry about making up a return for him?

A. I have had no reason to consult with him.

Q. Did you ever?

A. No, I never consulted with Mr. Newton Sherry about the preparation of any return.

Q. At no time? A. At no time.

Q. Were you acquainted with the S & P Company?

A. I had a pretty fair knowledge of the S & P Company.

Q. You did some work for them, did you?

(Testimony of James F. Murray.)

A. After 1943 when they were buying all these locations I took quite a few inventories for them on the purchase of these places; Keith Jones in particular and the Hollywood Recreation Center, too.

Q. To your knowledge, and I speak with respect to your knowledge only, do you know whether Mrs. Ferguson, then Margaret Sherry, took any part in the management of first S & P?

A. She had no part in the managing of S & P Company.

Q. Any at all? A. None.

Mr. Townsend: I move to strike that, your Honor. [127] I don't think this witness is qualified to answer that.

Mr. Carr: He was keeping the books at one time, I thought he said.

Mr. Townsend: Was he a member of the management of the company?

Mr. Carr: Go ahead.

Mr. Townsend: I'd prefer to ask him on what he bases that knowledge.

Mr. Carr: All right.

The Witness: After the S & P Company, which was owned by Mr. Kalmanovitz and Mr. Sherry, started to buy quite a few locations, they came to me and asked me to take inventories in these various places. I was in the S & P Company at least once or twice a week. I know that Mr. Newton Sherry or Miss Margaret Sherry had nothing to do with the management of the place.

Q. (By Mr. Carr): Did you keep the books or

(Testimony of James F. Murray.)
supervise them, or what?

A. No, I didn't keep the books for the S & P Company.

Q. Did you supervise?

A. I didn't supervise the books.

Q. You were just making up the separate inventories?

A. Various inventories at various times when they purchased various places, yes.

Q. Now, when was it first drawn to your attention that [128] there was a supposed partnership, Sherry Enterprises?

A. At the time right prior to September 30, 1943. I was told by Mr. Sherry that there was going to be a partnership formed for me to close the books of the Monticello Cafe, the Hollywood Cafe, and turn over the books and balance sheets to Mr. Don Hughes, which I did.

Q. And after this date, did you keep your offices at the same place?

A. That is correct, yes.

Q. And did you continue to do anything—any business with Mr. Sherry, Nathan Sherry?

A. I knew that the gift tax return was filed. I knew what businesses were in that gift tax return.

Q. What activity, if any, did you have with Mr. Sherry after this partnership document came into existence, that is, in 1943?

A. Mr. Sherry showed me those documents, Mr. Carr, but as far as having any activity business with Mr. Sherry, I went out to the S & P Company

(Testimony of James F. Murray.)

and he told me at various times what was going on, what they were doing, what places they were buying, and things like that.

Q. As far as you knew—strike that. Let me see if I can put it this way.

What, if anything, did you observe about the management of S & P during the years 1945 and —who was [129] managing it?

A. Mr. Kalmanovitz was the manager of the S & P Company at all times. I knew Mr. Kalmanovitz——

Q. You have answered my question.

Now, then, in 1946 who was managing?

A. Mr. Kalmanovitz.

Q. What part was Mr. Nathan Sherry playing, to your knowledge?

A. Mr. Nathan Sherry told me in 1946 that he——

Q. You are not answering the question.

A. Mr. Sherry told me——

Q. What you saw or what you heard.

A. Mr. Sherry did not manage S & P Company in any way. He was just there as a good fellow to meet customers and things like that.

Mr. Townsend: Your Honor, respondent moves to strike that. I don't believe it is based on this man's own observation.

The Witness: I testified, I think, counsel, I was in places once or twice a week, and I saw——

The Court: I will not strike it. Much of this witness' testimony is of an unsatisfactory char-

(Testimony of James F. Murray.)

acter, and I am going to have to read it in the light of the conclusions I form of his testimony. [130]

Q. (By Mr. Carr): Well, now, Mr. Murray, if you will just be specific. I think you will help us. All I want to know, if you know of your own knowledge, what Mr. Sherry did with respect to S & P enterprises during 1944 and '45.

A. Mr. Sherry——

Q. Nathan Sherry I am talking about.

A. Mr. Nathan Sherry during those particular years was just, you might as well say, a front man. He met the customers, and talked to the customers. That is all he did as far as managing the S & P Company.

Q. Now, then, with respect to Sherry Enterprises, did you ever see a set of books for Sherry Enterprises? A. I saw the tax returns.

Q. Did you ever see a set of books?

A. No, I saw the tax returns is all. The answer is no.

Q. You prepared whatever these tax returns that you have mentioned merely from partnership tax returns? A. That is correct.

Q. Without looking at any books?

A. That's right.

Q. Did you ever at any time during the time —strike that.

How often would you see Mr. Nathan Sherry say during 1944?

A. I saw Mr. Sherry once or twice a week, Mr. Carr. [131]

(Testimony of James F. Murray.)

Q. And were you discussing business matters with him?

A. He told me—no, I did not discuss business matters with Mr. Sherry as far as the S & P Company. He told me what was going on.

Q. I am talking about business matters, any business matters. A. No.

Q. And where were you located?

A. The Hollywood office on Vine Street.

Q. Did you ever at any time see Mr. Newton Sherry in that office?

A. I never saw him, never.

Q. In '44, '45, did you ever see Margaret Sherry or Margaret Ferguson in that office in 1944 or '45?

A. Never.

Q. Now, I will ask you a very specific and direct question. First of all, I will withdraw that.

You were a very good friend of Mr. Sherry, weren't you? A. That is correct.

Q. Now, irrespective of that friendship, I understand that you now realize you are under oath and you will state the facts?

A. That is correct, sir.

Q. I want to ask you this: Did Mr. Sherry ever indicate [132] to you by word of mouth that he was forming this partnership, Sherry Enterprises, for the purpose of splitting up his taxes?

A. No, never, Mr. Carr.

Q. Did he ever indicate to you in any way why he was doing it? A. Never.

Q. You never asked him?

(Testimony of James F. Murray.)

A. I never asked him.

Q. Were you interviewed, by the way, by Mr. Burns? A. I was, yes.

Q. Did he ask you or inquire along the same lines that I am asking you now about whether there was a partnership or not?

A. That is correct.

Mr. Carr: That is all.

Cross Examination

Q. (By Mr. Townsend): Mr. Murray, I believe you stated that you made out some partnership returns for Sherry Enterprises?

A. That is right.

Q. What years did you make out those returns?

A. Probably '47, '48, '49, around there.

Q. Any others besides that?

A. I'd have to check the file.

Q. I suppose you can remember now, '47, '48, '49—— [133]

A. Probably up to '50, counsel, I'd have to check the file to find out.

Q. When you prepared those returns, did you file those returns yourself?

A. During those years I would have to go back and look at the records. We did keep during those years a record of every tax return filed and how they were filed. I know we have for the past five years. Prior to that, I don't know if we mailed a tax return out. We had a record in the office. We have done that for the past four or five years,

(Testimony of James F. Murray.)

whether or not the office mailed them, I don't know.

Q. As far as you were concerned when you were preparing these partnership returns, you felt this was a bonafide partnership?

Mr. Carr: I object to that on the ground it asks for a conclusion of the witness, your Honor, what he felt. That is the issue in question here.

The Court: I assume he either felt that or he was bordering on to some dangerously unprofessional conduct.

Mr. Carr: That may well be true, but it wouldn't be material in this case what he felt. It wouldn't bind the Court in any way. That is my point.

The Court: I certainly wouldn't be bound by it.

Mr. Carr: I know you wouldn't as a lawyer, but at the same time I don't think the record should have that in it. [134]

The Court: I will sustain the objection.

Q. (By Mr. Townsend): Very well, your Honor, I will try to rephrase the question.

Was there anything in any way or any time which Mr. Sherry or anybody else said that would lead you to believe that this was a fictitious partnership?

A. I don't think anyone said at any time or led me to believe that it was a fictitious partnership.

Q. That it was a fictitious——

A. I don't think anyone said anything to that effect.

Q. There was nothing then that would lead you

(Testimony of James F. Murray.)

to believe that this was a fictitious partnership?

A. I can't say it was a fictitious partnership.

Q. I am not asking you that, Mr. Murray. I am asking you was there anything to lead you to believe it was a fictitious partnership?

A. I don't think it was a fictitious partnership.

The Court: You are not answering the question.

The Witness: No.

Q. (By Mr. Townsend): Now, when you prepared these individual returns, for Newton Sherry and for Margaret Sherry, are you telling me that you didn't ask them if they had any other additional income? [135]

A. No, I opened up a set of partnership books in 1947. We continued on with this partnership set of records.

Q. What partnership are you speaking of?

A. I am talking about a continuation of the Sherry Enterprises.

Q. All right.

A. When this thing started under investigation, I went and opened up a set of records during all the time Mr. Burns was investigating and for what information I could gather, I opened up these books and records.

Q. When would you have done that?

A. After this investigation started, I had to go back and try to pick up the information and everything.

Q. This investigation was going on after 1947?

(Testimony of James F. Murray.)

A. It started in '47, the latter part of '47—no, the first part of '47.

The Court: And there hadn't been any books before that?

The Witness: I didn't see any books before that, your Honor, because I opened up a new set of records from all the information I could gather as I went along. In other words, I started and I had to go back and pick up previous information, in the bank statements I could find. Anything I could find that could be entered into a set of books or records and attempt to build up a set of records.

Q. (By Mr. Townsend): Well, now, you say that you prepared some books, now, what did you use those books for?

A. What did I use them——

Q. You didn't use them to prepare those income tax returns?

A. After I opened those books and records the information I had in those books and records I used to prepare the tax returns.

Q. Let me point out to you that these tax returns were filed on March 15, 1947. Is it your testimony that the information contained on those comes from books that you recreated in 1947?

A. No, no, if you have listened to my testimony before, counsel, I prepared these returns from income tax returns that Mr. Hughes had prepared.

Q. I see, and by the way, when you spoke of Don Hughes, you meant Herndon Hughes?

A. Herndon Hughes, yes, sir.

(Testimony of James F. Murray.)

Q. And was it your testimony that you didn't talk to either Newton or Margaret Sherry—about these returns?

Mr. Carr: Now, counsel, let me suggest you say which returns because that is where the confusion came.

Mr. Townsend: I am speaking about Exhibit B. He has only prepared two returns as I understand.

Mr. Carr: I know, but you asked him if I *may so* about later years after '47 is when the books were set up.

Mr. Townsend: It is well taken.

Mr. Carr: So, he was confused, I think, about later years.

Q. (By Mr. Townsend): I am talking about Exhibit B and Exhibit D which are right in front of you, Mr. Murray, which are the returns which you prepared?

A. These tax returns were turned over to me by Yessner & Hughes pretty close to the filing time, and I had no time to ask anyone any questions. I just prepared these tax returns from the tax returns that Yessner & Hughes had filed.

Q. I see, and you did not ask these parties if they had any other additional income?

A. No, I did not.

Q. Now, directing your attention to Exhibit D and in doing, would you show or state for the record what the income is shown thereon?

A. Shows the S & P Company, $1950.00 and $19,156.65, a total of $21,106.85.

(Testimony of James F. Murray.)

Q. Where did you get the information about the $1950.00?

A. Not having the partnership tax return, I assumed I got it off the tax return that was filed by Yessner & Hughes.

Q. Let's take a look at that. [138]

A. I will correct that. That is a salary item. That is the salary item that probably came when he worked down in Wilmington.

Q. I see. Where did you get that information?

A. Oh, without going back to the file, I couldn't answer that question.

Q. I mean obviously it didn't come from the partnership returns prepared by Mr. Hughes, isn't that correct?

A. Unless that information was in the file that was turned over to my counsel.

Q. Now, did you represent either Mrs. Ferguson or Mr. Newton Sherry when Mr. Propeck, Revenue Agent, was making investigation?

A. No, sir, Yessner & Hughes recommended.

Q. Mr. Murray, did you act as a trustee for either of the petitioners here?

A. Oh, I think we did act as a trustee.

Q. What was the approximate—what was the property that you were trustee of?

A. That was the Clover Club.

Q. That was the Clover Club that Mr. Nathan Sherry got out of his break-up, split up with the S & P Company, is that correct?

A. Yes.

(Testimony of James F. Murray.)

Q. Now, what happened to that property? [139]

A. I think the Clover Club burned down.

Q. Now, you said you were trustee of that property? A. That is correct.

Q. Exactly who did you represent?

A. Who did I represent?

Q. Yes, as trustee, I mean. Who were the beneficiaries?

A. Well, Newton and Margaret Sherry were the beneficiaries, I assume, under that.

Q. And can you tell me approximately the amount of the assets of that trust as best you can recall? A. No, I can't recall.

Q. You don't recall? You have no recollection whatsoever? A. No.

Q. Do you know that a mortgage was held by that trust?

A. There wasn't—I don't think, Mr. Counselor, there was a mortgage held there by that trust.

Q. Now, did you ever distribute any assets or any particular income from that trust to either of the beneficiaries?

A. Of the beneficiaries?

Q. Yes. A. No.

Q. What happened to it?

A. I imagine Mr. Sherry got all that money.

Q. Well, were you—weren't you trustee? [140]

A. I assume that I was, yes.

Q. But you didn't do anything about it?

A. No.

Q. You didn't represent the beneficiaries in any

(Testimony of James F. Murray.)

way? A. No.

Q. As far as you know, the trust vanished, is that correct? A. That is correct.

Q. Now, when you spoke about these various places that you went out to take inventories, I assume you are talking about these various clubs here which would be in different parts of the city?

A. Restaurants and bars, yes.

Q. That would not be the office of S & P Company?

A. Nowhere in the office of S & P Company. I did take an inventory that was the Hollywood Recreation Center.

Q. But all those inventories were at places apart from there?

A. They were apart and most of the time Mr. Kalmanovitz and Mr. Sherry were present.

Q. Did you take any inventories off at any office of Sherry Enterprises?

A. No, only the one inventory at the time of the purchase we took there, the Hollywood Recreation, that is for—that is where the office was. [141]

Q. The office of Sherry Enterprises?

A. Was in the Hollywood Recreation. I took the original inventory.

Q. You were only there once?

A. Only as far as doing any business, yes.

Mr. Townsend: I have no further questions.

Redirect Examination

Mr. Carr: May I ask one or two further questions?

(Testimony of James F. Murray.)

Q. (By Mr. Carr): You were pretty well acquainted with Mr. Nathan Sherry?

A. About 38 years.

Q. Where did Mr. Sherry come from?

A. Baltimore, Maryland.

Q. What was his business?

A. Mr. Sherry at that time was in the newspaper business.

Q. He was a circulation builder?

A. Circulation man, that is right.

Q. He moved over to Chicago and helped build circulation there? A. Seattle.

Q. Those were the good old strong armed days, circulation strong arm days?

A. That is right. [42]

Q. Mr. Sherry was a rather domineering type of man, was he? A. He was.

Q. And if Mr. Sherry told the children to do something, did they usually do it?

A. They did it.

Q. Was there ever any questions asked?

A. Never any question asked.

Q. As a matter of fact, when Mr. Sherry was around his place of business with you folks, did any of you question him?

A. No, we never questioned him.

Q. When he asked you to do something, what was done?

A. Mr. Carr, if you are speaking as far as his children are concerned, I'd say when he asked them to do anything, they did it.

(Testimony of James F. Murray.)

Q. Well, did he ask them or tell them?

A. He told them to do it.

Q. When he told his employees, would he ask them or tell them?

A. No, he told them what to do. He didn't ask them any questions.

Mr. Carr: I think that is all.

Recross Examination

Q. (By Mr. Townsend): Mr. Murray, did you live with the Sherry's at any [143] time?

A. Back in 1937 I think we lived with Mr. Sherry in Westwood for probably nine months, I'd say, counsel.

Q. Other than that period——

A. No, we never lived with them. I knew him very well, but I never lived with him.

Q. I take it from this period in 1943 there on in, you were self-employed?

A. I was in business for myself.

Q. You had other clients besides Mr. Sherry?

A. That is right.

Mr. Townsend: That is all.

Mr. Carr: That is all. Thank you very much. May he be excused?

The Court: Yes.

(Witness excused.)

Mr. Carr: That finishes petitioner's case, your Honor.

Mr. Townsend: Respondent calls Mr. Burns.

Whereupon,

WILLIAM B. BURNS

called as a witness for and on behalf of the Respondent, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your name and address [144] for the record, please?

The Witness: William B. Burns, B-u-r-n-s, San Marino, California.

Direct Examination

Q. (By Mr. Townsend): What is your position, Mr. Burns?

A. I am with the Intelligence Division of Internal Revenue Service.

Q. And what was your position in November of 1949?

A. I was a special agent of the Intelligence Unit, as it was called at that time.

Q. And what connection have you had with this case?

A. It was assigned to me for investigation as special agent, a joint investigation with Internal Revenue Agent Gordon B. Keller.

Q. During your investigation of that case, did you have any occasion to take sworn statements of either of the petitioners here?

A. Yes, I did, sir.

Q. Did you take such a statement of Mr. Newton Ivan Sherry? A. Yes, sir.

Q. Do you recall the date of that?

(Testimony of William B. Burns.)

A. Not exactly but it was in the fall of '49.

Q. And where was that statement? [145]

A. Room 844 of this building.

Q. Of this building, and was Mr. Sherry under oath at that time? A. Yes, sir.

Q. At that particular question-and-answer statement, was this question asked by you and did Mr. Newton Ivan Sherry answer as follows:

"Q. Are you a partner in the partnership known as Sherry Enterprises? A. I am."

Mr. Carr: I will stipulate, counsel, and save you the time that the answers made in that document were made by Mr. Newton Sherry, to save you reading them, and have the witness testify. I assume that you represent that that is a correct document and upon your representation I will so stipulate.

Mr. Townsend: Yes, sir.

Mr. Carr: If that is satisfactory.

Mr. Townsend: You want the document to go in?

Mr. Carr: No, no, no, I meant you could read them without putting the questions to the witness.

Mr. Townsend: Oh, fine.

Q. (By Mr. Townsend): The next question was asked by Mr. Burns and answered by Mr. Newton Ivan Sherry: [146]

"Q. In your opinion, what was the purpose of the formation of Sherry Enterprises partnership?

"A. Well, the formation, in other words, is between all of us. The money was put in in case anything should happen to my dad, we would still have

(Testimony of William B. Burns.)

a partnership, there was money that was left to us that made up the partnership. Also, there was money I invested that made up the partnership."

The following question was asked by Mr. Burns and answer given by Mr. Newton Ivan Sherry:

"Q. Since the formation of Sherry Enterprises has there ever been a meeting of all the four partners in which business policies and plans were discussed?

"A. Well, at different times, if ever we wanted any type of business whatsoever added to the Sherry Enterprises, we would all get together and have a mutual agreement."

That completes the questions and answers, and I believe our stipulation is that those questions were asked and the answers were as given by Mr. Newton Ivan Sherry.

Mr. Carr: So stipulated.

Mr. Townsend: With that, I am through with this witness. [147]

Cross Examination

Q. (By Mr. Carr): Just a couple of questions.

Mr. Burns, I believe you and I have met before, haven't we, Mr. Burns?

A. We have, yes, sir.

Q. And, Mr. Burns, you were on this investigation for a long time, weren't you?

A. Not as we consider a long time.

Q. How long a time, approximately?

A. Well, we started it in 1947, and it is still

(Testimony of William B. Burns.)

going on, I believe, it could be successfully said. This is '57.

Q. Mr. Burns, when you first started out investigating this case, you were proceeding on the theory that there was an invalid partnership, is that right?

A. We endeavored to proceed on no theory. We endeavor to gather facts. I had no preconceived theory as to the case until we had completed our report.

Q. Well, perhaps I put it wrongly. Weren't you pursuing or at least making the effort to obtain from the Sherry's, Nathan Sherry, these two children, this girl and boy, the fact that this was a fictitious partnership? Weren't you making that effort at the time to establish that fact?

A. No, sir, I was endeavoring to get the facts, sir. [148]

Q. But you were pressing very hard on the proposition as to whether or not it was a valid partnership, weren't you, in fact?

A. No harder on that than on any other fact involved in the——

Q. Well, if you remember at what time did you decide in your own mind that there was actually a partnership?

A. I would not be able to fix that definite point of time. I don't believe I could, Mr. Carr.

Q. Well, now, you went to trial in the criminal case in 1952.

A. It would be prior to that.

(Testimony of William B. Burns.)

Q. That was about August of 1952?

A. I assume you are correct in that regard.

Q. And you testified in that case, did you not?

A. I believe I did, yes. I know I did.

Q. At some length, and you testified as to your findings, did you not, respecting partnership matters? A. Yes.

Q. And at that time you did not testify either way, that you had found a partnership or had not found a partnership, is that correct, or do you remember?

A. My present recollection doesn't include any testimony concerning the validity or non-validity of that partnership. [149]

Q. When you were questioning this boy, Newton Sherry, did he have counsel with him?

A. He did, sir.

Q. And who was his counsel?

A. Conrad Hubner.

Q. And you were questioning him about many other things in addition to this partnership, is that correct? A. Yes.

Q. And at that time you also questioned the girl and took her statement, or close to that?

A. Yes.

Q. And you questioned her about this partnership? A. Yes.

Q. Now, here is what I am coming to. During the questionings, you ofttimes have little off-the-record discussions, don't you?

(Testimony of William B. Burns.)

A. I would not say ofttimes, occasionally, sometimes, yes, sir.

Q. In other words, you reach a point when you are taking a statement when you say, "Off the record for a few moments" and you discuss something. Did you do that in this particular case when you were taking the statement of Newton Sherry?

A. I'd have to refresh my recollection to answer that whether it took place or not. It would be my guess that it [150] did if you want my guess.

Q. Well, I will take your guess, and I take it that guess is based on some recollection, some maybe faint recollection in your mind?

A. No, sir, not particularly as to that interview, but as to what happens in most interviews.

Q. Well, let me see if I can refresh your recollection. Do you recollect that when you were discussing the partnership feature with Mr. Newton Sherry on an off-the-record discussion that you made the statement, in substance and effect, I don't know that these are exact words: Now, Mr. Sherry, you know that that partnership was set up for only one purpose, that was to avoid tax. Do you remember making a similar statement?

A. I do not.

Q. You don't remember him making an answer that his father told him that it was set up to protect the children?

A. Well, that answer is recorded. I am quite sure.

Q. You don't remember the other part? Do you

(Testimony of William B. Burns.)

ever remember hearing the daughter or Newton make that statement in answer to a question by you or a statement by you that wasn't it a fact that this partnership deal was phony. It was set up purely for the purpose of avoiding taxes?

A. You have got several things in there.

Q. Maybe I have. I will clarify that.

Do you ever remember a statement made by you to [151] Margaret Sherry at which time you said, in effect, Now, you know that this partnership is phony. It was set up only for the purposes of evading taxes or avoiding taxes, and she said, in substance and effect, "Well, I don't know much about it, but my dad told me it was set up for the purpose of protecting us children."

A. Now, what is your question?

Q. Did you ever remember that occurring?

A. No, sir.

Q. Never occurred to your knowledge?

A. There is a recorded statement by her, and I believe also by Mr. Newton Sherry to the effect that the partnership, one of the reasons for the existence of the partnership, was for the protection of their interests.

Q. How many times would you say you talked to Margaret Sherry that was not recorded?

A. How many times?

Q. Yes.

A. Something less than five, I would think.

Q. More than two but less than six?

A. I think more than two.

(Testimony of William B. Burns.)

Q. And how many times would you say you talked to Newton Sherry when those conversations were not recorded?

A. Oh, that is very difficult for me to recall definitely. [152]

Q. Just give me an approximation.

A. But——

Q. Approximately.

A. I can recall at the moment just once, but there may have been one or two other times.

Q. Well, I am just about finished. Do you recollect having two or three conversations with Mr. Newton Sherry and then him bringing this lawyer to give the statement at the time it was given under oath?

A. Your question is do I recollect having talked with him before the statement was taken?

Q. Yes, before he brought a lawyer in?

A. I'd have to refresh my recollection from my notes to be sure as to that.

Q. Mr. Burns, let me ask you this: Don't you recollect saying something to the effect that if this was a phony partnership that it would, in effect, be a conspiracy?

A. This I do recollect, Mr. Carr, that I never used the word "phony" with regard to the partnership.

Q. All right. Did you ever indicate in any way by word of mouth to Mr. Newton Sherry that if this partnership was formed for the purpose of evading

(Testimony of William B. Burns.)

taxes, that he, himself, might find himself in trouble?

A. That I said that to Mr. Sherry, I have no recollection. I very seriously doubt that I did. [153]

Q. You didn't give him anything as far as you remember, anything to believe that he might be in trouble because of this alleged partnership, this splitting of income?

A. No, not—I certainly have no recollection whatever, and if I recall, Mr. Carr, I made an explanation both to Miss Margaret Ferguson and I believe Mr. Newton Sherry, but at least Mrs. Ferguson, were used as government witnesses in the trial, as I recall.

Q. They were subpoenaed, weren't they?

A. They were used as witnesses. How they were secured, I just can't be sure.

Q. Well, then, I take it, Mr. Burns, concluding that I can rest assured that you said nothing at any time which would lead either one of these—Mrs. Ferguson or Mr. Newton Sherry to believe that they were under investigation themselves?

A. I am in no position to testify as to what something I may have said caused them to reach a conclusion.

Q. Were you investigating them at the time?

A. As partners of Sherry Enterprises?

Q. You are attached to the Special Intelligence Unit, aren't you? A. I was, yes, sir.

Q. And they handle criminal matters, don't they?

(Testimony of William B. Burns.)

A. As well as tax matters, yes, sir.

Q. But it doesn't usually come into your hands until [154] it gets in the fraud?

A. But in the course of that investigation, I call attention to the fact that it was a joint investigation, and at that time I was working jointly with Internal Revenue Agent Keller.

Q. But you were in charge?

A. Technically, yes.

Q. And the thing I am trying to find out, were you investigating Newton Sherry and Margaret Sherry at the same time you were investigating Mr. Nathan Sherry?

A. I suppose that could be answered affirmatively, yes, sir.

Mr. Carr: That is all.

Redirect Examination

Q. (By Mr. Townsend): Just one or two questions. Now, Mr. Burns, during your examination you were primarily interested in digging out the facts, is that correct? A. Yes, sir.

Q. Now, on the basis of your examination of this entire case, did you make any recommendation as to whether or not this partnership should be recognized? A. I did, sir.

Q. And what was that recommendation?

A. That it be recognized. [155]

Q. And what was that recommendation based upon?

A. There were at that time a number of family

(Testimony of William B. Burns.)

partnership decisions. I can't just at the moment recall the nature of them. There were two leading cases that were settled at about that time. I just can't recall the name of them.

Q. Was it also based on the examination and the fact that you had—that were disclosed to you during the examination? A. Yes, sir.

Mr. Townsend: I have no further questions.

Recross Examination

Q. (By Mr. Carr): Now, Mr. Burns, you say you recommended that the partnership be recognized, what date?

A. You mean what date did I make that recommendation?

Q. Yes.

A. It would be the date of my final report. I can't just recall that at the moment. I can refresh my recollection in a few minutes if you wish me to.

Q. That was before the criminal trial, wasn't it?

A. The report was written before the criminal trial, yes, sir.

Q. Isn't it a fact that the reason you made that recommendation was to eliminate that from the criminal case [156] so that there would be no question involved of partnership in the trial of the criminal case?

A. That is not the reason.

Q. At any time, did any of the children have any basis like that at all?

(Testimony of William B. Burns.)

A. It might have been, probably was one of the facts that entered into the consideration.

Q. Isn't it a fact, Mr. Burns, that you discussed this very feature with your associates, and in discussing it said, in effect, I wasn't there, but I am going to guess, in effect, we better eliminate this partnership issue because we have got plenty else on the man and we don't want to get all his partnership involved in the criminal trial. Isn't that about the substance of it?

A. Well, I don't think so.

Q. Well, now, you say you don't think so. It is pretty close, isn't it?

A. We considered it both ways, of course, but the facts were overwhelming, and the testimony was complete that a partnership did exist.

Q. I am just about finished, and I don't want to pin any bouquets on myself, but didn't you at that conference say well, this fellow Carr——

A. Which conference are you speaking of?

Q. When you were speaking of or discussing the [157] partnership in the criminal case, this fellow Carr will get a hold of that partnership and he will wind it up in a knot and give us trouble. Let's get it out of the criminal case.

A. I could not—it could not have been because you were not the attorney at the time.

Q. It wasn't about not winding it up in the criminal case?

A. No, we didn't discuss it from that standpoint.

(Testimony of William B. Burns.)

Q. You discussed it from the point of view that it would complicate the criminal prosecution?

A. No, sir.

Q. Not at all? A. No, sir.

Q. Just made it up solely on the merits and said we have concluded there was a partnership?

A. Yes, sir.

Q. How much time did you spend trying to prove that there wasn't a partnership?

A. I spent no time trying to prove anything in our investigations, Mr. Carr.

Q. You were just out to find out the truth?

A. That's right.

Mr. Carr: That is all.

Mr. Townsend: That is all.

Mr. Carr: Are you finished, counsel? [158]

Mr. Townsend: Just one thing. At this time respondent offers Exhibit K and L for identification in evidence.

Mr. Carr: Are those the signed——

Mr. Townsend: Yes.

Mr. Carr: We have no objection.

The Court: May be admitted.

The Clerk: Exhibits K and L.

(The documents above-referred to were received in evidence and marked Respondent's Exhibits K and L.) [159]

* * * * *

[Endorsed]: T.C.U.S. Filed May 8, 1957.

[Endorsed]: No. 16109. United States Court of Appeals for the Ninth Circuit. Margaret Lillian Ferguson, Newton Ivan Sherry and Lois Sherry, Petitioners, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed: July 22, 1958.

Docketed: July 24, 1958.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 16109

MARGARET LILLIAN FERGUSON,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

NEWTON IVAN SHERRY and LOIS SHERRY,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

STATEMENT OF POINTS ON WHICH APPELLANTS INTEND TO RELY

Appellants hereby state that the points on which they intend to rely on the appeal in this action are as follows:

1. The findings of fact, conclusions of law, and decisions of the Tax Court of the United States are not supported by the evidence.

2. The decisions of the Tax Court of the United States are contrary to law.

3. Errors occurred at the trial in the admission and rejection of evidence.

Dated at Los Angeles, California, this 23rd day of July, 1958.

/s/ CHARLES H. CARR,
Attorney for Petitioners

Affidavit of Service by Mail attached.

[Endorsed]: Filed July 24, 1958. Paul P. O'Brien, Clerk.

[Title of Court of Appeals and Cause.]

APPELLANTS' DESIGNATION OF RECORD ON APPEAL

Pursuant to Rule 75, Federal Rules of Civil Procedure, and Rule 17 of the Rules of this Court, the appellants, Margaret Lillian Ferguson, Newton Ivan Sherry, and Lois Sherry, hereby designate the parts of the record on appeal which they consider necessary for the consideration of the points on which they intend to rely on the appeal. (For the convenience of the Clerk, the document numbers referred to hereinafter are the document numbers supplied to this Court by the Clerk of the Tax Court of the United States in his transmittal letter of July 17th, 1958.)

1. Docket entries, Case No. 56085 (Document No. 1).

2. Docket entries, Case No. 56086 (Document No. 2).

3. Petition, Case No. 56085 (Document No. 3).

4. Answer, Case No. 56085 (Document No. 5).

5. Reply, Case No. 56085 (Document No. 6).

6. Petition, Case No. 56086 (Document No. 8).

7. Answer, Case No. 56086 (Document No. 10).

8. Reply, Case No. 56086 (Document No. 11).

9. Minutes of proceedings before the Tax Court of the United States (Document No. 16).

10. Stipulation of Facts, with Respondent's Exhibits A through J attached (Document No. 17).

11. Official record of proceedings before the Tax Court of the United States (Document No. 19), eliminating therefrom: Pages 1 to 6, inclusive; Lines 1 to 8, page 7; Page 159, line 12 to bottom of page; and Pages 160 to 164, inclusive.

12. Respondent's Exhibits K, L, and M, admitted in evidence (Document No. 18).

13. Memorandum Findings of Fact and Opinion (Document No. 23).

14. Decision, Case No. 56085 (Document No. 26).

15. Decision, Case No. 56086 (Document No. 27).

16. Petition for Review (Document No. 28).

17. Designation of Contents of Record on Review (Document No. 29).

Dated: July 23rd, 1958.

/s/ CHARLES H. CARR,
Attorney for Petitioners

Affidavit of Service by Mail attached.

[Endorsed]: Filed July 24, 1958. Paul P. O'Brien, Clerk.

[illegible]

[illegible]

[illegible] Court of Appeals

[illegible]

[illegible]

[illegible] Lois Sherry

[illegible],

Petitioner,

vs.

[illegible] Commission,

Respondent.

[illegible] Appellants Margaret [illegible], Respondent [illegible] Ivan Sherry and Lois Sherry.

[illegible] Cole

[illegible] Building

[illegible]

[illegible]

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PAUL P. O'BRIEN

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No. 16109

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

MARGARET LILLIAN FERGUSON, NEWTON IVAN SHERRY and LOIS SHERRY,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Brief for Appellants, Margaret Lillian Ferguson, Newton Ivan Sherry and Lois Sherry.

This is an appeal from decisions of the Tax Court of the United States in the cases of Margaret Lillian Ferguson v. Commissioner of Internal Revenue, and Newton Ivan Sherry and Lois Sherry v. Commissioner of Internal Revenue, entered on May 19, 1958 [R. 61, 62*], following a trial before the Tax Court of petitions for redetermination of deficiencies set forth by the Commissioner of Internal Revenue in Notices of Deficiency dated October 28, 1954 [R. 5-17, 26-36].

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*References to the printed Transcript of Record are referred to herein as "R." followed by the page numbers to which reference is made.

Jurisdictional Statement.

(1) The jurisdiction and venue of this Court to review the decisions in question is provided in Title 26, *United States Code,* Section 7482.

(2) The pleadings necessary to show the existence of jurisdiction are:

(a) Petition of Margaret Lillian Ferguson [R. 5-17]; Answer of Commissioner [R. 17-23]; Reply of Margaret Lillian Ferguson [R. 24-25];

(b) Petition of Newton Ivan Sherry and Lois Sherry [R. 26-36]; Answer of Commissioner [R. 37-43]; Reply of Newton Ivan Sherry and Lois Sherry [R. 43-45];

(c) Memorandum Findings of Fact and Opinion of the Tax Court of the United States [R. 49-61];

(d) Decision of the Tax Court of the United States in the case of Margaret Lillian Ferguson [R. 61];

(e) Decision of the Tax Court of the United States in the case of Newton Ivan Sherry and Lois Sherry [R. 62];

(f) Petition for Review [R. 63-65];

(g) Statement of Points on which Appellants Intend to Rely [R. 198-199].

Statutes Involved.

Internal Revenue Code, 1939, as amended, Title 26, *United States Code,* Section 181:

> "Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity."

Internal Revenue Code, 1939, as amended, Title 26, *United States Code,* Section 182:

> "In computing the net income of each partner, he shall include, whether or not distribution is made to him—

"(a) As part of his gains and losses from sales or exchanges of capital assets held for not more than 6 months, his distributive share of the gains and losses of the partnership from sales or exchanges of capital assets held for not more than 6 months.

"(b) As part of his gains and losses from sales or exchanges of capital assets held for more than 6 months, his distributive share of the gains and losses of the partnership from sales or exchanges of capital assets held for more than 6 months.

"(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b)."

Internal Revenue Code, 1939, as amended, Title 26, *United States Code,* Section 183(a):

"The net income of the partnership shall be computed in the same manner and on the same basis as in the case of an individual . . ."

Internal Revenue Code, 1939, as amended, Title 26, *United States Code,* Section 3797(2):

"The term 'partnership' includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation; and the term 'partner' includes a member in such a syndicate, group, pool, joint venture, or organization . . ."

Question Presented.

During the fiscal years ending June 30, 1945, and June 30, 1946, was there a *bona fide* and valid partnership, for the purposes of taxation, among appellants, their father, and their stepmother?

Specification of Errors Relied Upon.

(1) The Findings of Fact, Conclusions of Law, and Decisions of the Tax Court of the United States are not supported by the evidence.

(2) The Decisions of the Tax Court of the United States are contrary to law.

Summary of the Evidence

Petitions for redetermination of deficiencies and penalties were filed with the Tax Court of the United States by Margaret Lillian Ferguson and by Newton Ivan Sherry and his wife, with respect to income taxes of Margaret Lillian Ferguson for the calendar years 1944, 1945, and 1946, and with respect to income taxes of Newton Ivan Sherry and Lois Sherry, his wife, for the calendar years 1945 and 1946.

It was stipulated by the Commissioner that the deficiencies alleged were not due to fraud, and that the penalties for fraud were not applicable [R. 47]. It was also stipulated that the statute of limitations had expired for the year 1944 [R. 47], thus leaving in issue the years 1945 and 1946 in each case. It was also stipulated as follows:

> "The only issue with respect to income is whether or not these petitioners are taxable on a distributable share of the income of Sherry Enterprises, since petitioners Margaret Lillian Ferguson and Newton Ivan Sherry contend that they were not partners in Sherry Enterprises. Petitioners do not contest respondent's determination that the net worth statements set forth in the notices of deficiency reflect the income of Sherry Enterprises for the fiscal years 1945 and 1946, because they state they have no knowledge or information regarding the same" [R. 47].

Since there was but a single issue, involving identical years, the two petitions were consolidated for trial [R. 109].

Newton Ivan Sherry (hereinafter referred to as Newton) and Margaret Lillian Ferguson (hereinafter referred to as Margaret) are the son and daughter of Nathan Sherry, deceased [R. 47]. Lois Sherry was the wife of Newton Sherry during the years in question [R. 47], but is now separated from him [R. 87], and her only connection with the issue is that she filed joint returns with Newton [R. 50]. Lucille Lawler Sherry was the wife of Nathan Sherry and the stepmother of Newton and Margaret [R. 47]. The mother of Newton and Margaret died in 1937 [R. 151].

Throughout the period relevant to this proceeding Nathan Sherry possessed a power of attorney to act in behalf of Newton and Margaret [R. 53].

Commencing in December, 1940, Nathan Sherry and one Paul Kalmanovitz became associated as partners in business, becoming known as the S & P Company in 1941 or 1942 [R. 157]. The partnership operated various bars and nightclubs in Los Angeles, San Francisco, Oakland, and Pasadena [R. 158]. Kalmanovitz and Nathan Sherry were the principal partners, except that for a while they had additional partners in some of the individual enterprises [R. 158]. In 1947, following a disagreement, the partnership was terminated [R. 160-161] and Kalmanovitz took all of the partnership assets with the exception of seven lots on La Cienega and the Clover Club building and real property, which were distributed to Nathan Sherry as his share of the assets [R. 161].

In January, 1940, Newton (then approximately twenty years of age) joined the Marine Corps, in which service

he remained until his discharge in May, 1945 [R. 90]. Margaret enlisted in the Waves, a branch of the Navy, in February, 1943, and remained in the service until November, 1945 [R. 110]. She was twenty years of age at that time [R. 151].

In 1943, Nathan Sherry discussed with his accountant, Herndon Hughes, and an attorney, George Williams, now deceased, the formation of a family partnership [R. 68]. Nathan Sherry and his second wife were apparently not getting along very well together during this period [R. 154]. Nathan Sherry discussed with his accountant and attorney his family problems at some length and his desire to protect his children; and the idea of a family partnership developed at this conference [R. 77]. Mr. Williams thereafter drafted the partnership agreement [R. 68; Ex. G], and Mr. Hughes drafted gift tax returns [R. 69; Exs. I and J].

The purpose of the partnership, as discussed by Nathan Sherry with his accountant and his attorney, was an *effort to divide his estate, rather than his income,* and to protect his children by so doing [R. 77-78]. The tax advantage was discussed [R. 77]. Only a part of his property interests was included in the agreement [R. 79].

Prior to the death of their mother in 1937, Margaret and Newton were informed by her that she was leaving $20,000.00 to them [R. 105]. Nathan Sherry later told Margaret that he was holding that money for her and for Newton [R. 128-129]. According to the Articles of Copartnership [Ex. G], and the gift tax returns [Exs. I and J], the interests in property purportedly conveyed to Newton and Margaret as their portion of the partnership came entirely from the community property of Nathan Sherry

and his wife, Lucille Lawler Sherry, stepmother of Newton and Margaret, and were acquired subsequent to their marriage on April 1, 1938.

At the time the partnership agreement and gift tax returns were drafted, both Newton and Margaret were away from home in the armed services [R. 90, 110]. No discussions were had with either of them before or during the drafting of these instruments [R. 69-70].

The partnership agreement was signed by Newton while serving as a sergeant in the Marine Corps on Guadalcanal [R. 86; Ex. G]. His father sent him the document with the request to sign it and mail it back, which he did [R. 87]. Newton did not read the document when he signed it [R. 86-87]. Newton considered his father a very aggressive man, and always did what he told him to do, whether right or wrong [R. 107-108]. The donee's return with respect to the purported gift [Ex. I] was not presented to Newton, but was signed by his father as attorney-in-fact.

The partnership agreement [Ex. G] was signed by Margaret while she was serving in the Waves at Dayton, Ohio [R. 111]. It was signed on the instructions of her father [R. 110-111]. She was never consulted by her father, her stepmother, or her brother with respect to the agreement [R. 111]. She signed the gift tax returns [Exs. I and J], but does not recall the fact, or of having read them [R. 114]. She had no discussion with anyone relative to the formation of a partnership [R. 113].

When Newton was returned to this country from Guadalcanal, he was first sent to a hospital in Philadelphia, where he learned lipreading to correct deafness before his discharge [R. 86-87]. After his discharge in May, 1945,

he attended college until November, 1945, and went to work as manager of a drive-in and bar owned by S & P Company at $110.00 per week [R. 91-92]; then he went back to house painting for a while, and also worked for Le Fleur de California, a perfume business owned by his father [R. 97-98]. At the time of the trial, his employment was that of a house painter for wages [R. 85]. He never conducted any business for Sherry Enterprises partnership [R. 89], nor supplied any of the funds used to pay taxes on income reported from Sherry Enterprises [R. 89]. He had nothing to do with the preparation of tax returns for 1945 and 1946 [R. 89], or with the books, records, or returns of Sherry Enterprises [R. 90-91]. The returns were signed by him at the request of his father [R. 96]. The returns were prepared by an accountant at the request of Nathan Sherry, without consultation with Newton, and the checks in payment of the taxes shown thereon were issued by Nathan Sherry [R. 167-168].

The partnership returns for Sherry Enterprises for the fiscal years beginning July 1, 1944, and ending June 30, 1945, and beginning July 1, 1945, and ending June 30, 1946, respectively, were signed by Nathan Sherry and filed with the Collector of Internal Revenue [Exs. E and F]. Neither Margaret nor Newton examined, signed, or had anything to do with the preparation of these returns [R. 71, 74]. They were prepared and filed under the direction of Nathan Sherry [R. 70].

In 1946, Newton purchased a home for $8,599.00, the money being furnished to him by his father; the house was sold later in the same year and the money returned to his father [R. 98]. Newton did not consider the house as belonging to himself, but as an asset of Sherry Enterprises [R. 100].

Newton Sherry did not at any time receive any funds from the Sherry Enterprises partnership [R. 89].

Margaret Ferguson was discharged from the Navy in November, 1945 [R. 110], and then attended the University of Southern California from January 2, 1946, to June, 1946 [R. 122-124]. Commencing in September or October, she was employed by Sherry-Dunn, a perfume business owned by her father, until she was married the following March [R. 129-130]. She answered the telephone, took messages, and performed similar tasks [R. 130]. She understood that Sherry-Dunn was a part of Sherry Enterprises [R. 130-131]. During this period, she lived at home with her father, and had a joint bank account with him, on which she drew for household expenses [R. 118]. She also ran errands for her father, occasionally making deposits and cashing checks [R. 117]. She did nothing to help manage the partnership [R. 117], was not consulted as to policy [R. 118], and was not even given a chance to voice opinions [R. 119]. She never received any of the income from Sherry Enterprises [R. 122] or supplied any of the money to pay taxes on the income from Sherry Enterprises reported on her returns [R. 122]. The accountants who prepared the individual returns for Newton and Margaret did so at the request of Nathan Sherry and without consultation with either Newton or Margaret [R. 69-73, 165-167] and the checks to pay the taxes were issued by Nathan Sherry.

When Margaret returned from the service, she received a check for $500.00 from her grandmother's estate, which she turned over to her father, who said he would put it in the business [R. 119-120], but did not say which business [R. 120].

In 1945 and 1946, some lots on Santa Monica Boulevard and a building were placed in the name of Margaret, or in the name of Marton Holding Company (the record is not clear as to which). Marton Holding Company was a corporation set up by Nathan Sherry with the explanation that he desired to protect his children [R. 130-131]. Margaret did not consider the properties as belonging to her, and believed that they were a part of Sherry Enterprises [R. 131]. The final disposition of this property does not appear in the record.

In 1947, Margaret was given stock in Marguery Corporation, which operated Lucy's Restaurant [R. 134-135]. At the time of the trial, she was manager of this restaurant [R. 135]. She considered this to be her property when received [R. 136]. Her father used funds of Sherry Enterprises to purchase the stock [R. 136]. The stock is worthless [R. 139].

At the time of the trial, Margaret was the owner of an apartment house at 647 North Irving Boulevard, Los Angeles, which was given to her by her father [R. 136-137]. The property is valued at $14,000.00 [R. 138-139]. She does not know where the funds came from to purchase it [R. 137].

At the time of the trial, Margaret was the record owner of a triplex at 1810 Courtney Avenue, which she acquired from Sherry Enterprises in 1950 [R. 138]. Its approximate value is $35,000.00, and Margaret has made and is making the mortgage payments on the property [R. 138].

Newton and his wife signed a "Waiver of Restrictions" on the Assessment and Collection of Deficiency in Tax dated July 19, 1948, for the year 1945, agreeing to additional tax in the amount of $1,114.42 [Ex. K]. Newton

testified that when he signed it, he did not understand it, but signed at his father's request [R. 101].

Margaret signed a "Waiver of Restrictions on the Assessment and Collection of Deficiency in Tax" dated July 19, 1948, for the year 1945, agreeing to additional tax in the amount of $1,109.75 [Ex. L]. Margaret testified that she had no recollection of signing the document, but that "all of these things were presented to me to sign, and I never knew. I took them to be correct and I signed them" [R. 140].

On November 2, 1949, in the course of the investigation of Nathan Sherry by the Intelligence Unit, Newton testified that on that date he was a partner in Sherry Enterprises [R. 103-104]. Before the Tax Court, Newton testified that he had given such testimony to the Special Agent "because it was wrote up as a partnership" [R. 104]. ". . . Well, considering yourself and participating and receiving funds out of it that you can put in the bank and keep, it's a different thing" [R. 103].

On May 15, 1950, in the course of the same investigation, Margaret testified under oath that she was at that date a partner in Sherry Enterprises [Ex. M]. She based her statement that she felt there was a partnership upon the fact that her father told her there was a partnership [R. 143]. Nathan Sherry was indicted for criminal tax evasion and was tried on the charges in August of 1952 [R. 145]. Up to the time of the trial of her father, Margaret had never seen a copy of the 1945 or 1946 partnership returns [R. 112].

Up until the time of the dissolution of S & P Company in 1947, Paul Kalmanovitz never heard of Sherry Enterprises [R. 157], nor was he ever notified that Sherry Enterprises owned any part of S & P Company [R. 158].

Neither Newton nor Margaret ever took any part in the management of S & P, nor did they take part in the negotiations relative to dissolution [R. 158-161].

One of the former S & P properties taken by Nathan Sherry upon dissolution of that company was the Clover Club and its underlying real property [R. 161]. This property was put in trust by Nathan Sherry for the benefit of Margaret and Newton [R. 179-180]. The Clover Club burned down [R. 180], the property was sold, and Nathan received all of the proceeds [R. 180]. The trust vanished, with the beneficiaries receiving nothing [R. 180-181].

Newton and Margaret never asked to examine, or examined, any books or records of Sherry Enterprises or of S & P [R. 90-91, 122, 158]. Neither Newton nor Margaret had anything to do with the preparation either of the partnership returns involved [R. 71] or of their own personal returns [R. 71-74, 166-168].

Partnership books were first compiled in 1947, after the investigation by the special agent of the Treasury Department had commenced [R. 176].

On the basis of the above evidence, the Tax Court held that Newton and Margaret were partners in Sherry Enterprises for the fiscal years ended June 30, 1945, and June 30, 1946, respectively [R. 58], and accordingly rendered decisions against them [R. 61-62].

Argument.

We are concerned here with the sole question of whether or not there existed among appellants, their father, and their stepmother, during the fiscal years ended June 30, 1945, and June 30, 1946, a *bona fide* and valid partnership for the purposes of taxation.

The standard by which an alleged "family partnership" is to be measured was laid down by the Supreme Court in the now famous case of *Commissioner v. Culbertson* (1949), 337 U. S. 733, 93 L. Ed. 1659. At page 742 of that case the Court stated:

> "The question is not whether the services or capital contributed by a partner are of sufficient importance to meet some objective standard supposedly established by the Tower case, but whether, considering all the facts—the agreement, the conduct of the parties in execution of its provisions, their statements, the testimony of disinterested persons, the relationship of the parties, their respective abilities and capital contributions, the actual control of income and the purposes for which it is used, and any other facts throwing light on their true intent—the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise."

Applying the language of the *Culbertson* case, therefore, for the purpose of determining the ultimate question of whether "the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise," we find the following evidence applicable:

(a)". . . considering . . . the agreement":

The agreement was drawn entirely at the dictation of the father (Nathan), without consultation with either of the appellants; was signed by them on his orders, when each was away from home in the armed services during time of war; and appellants were later informed that it was only a method of protecting them in the event of their father's death.

(b) ". . . the conduct of the parties in execution of its provisions . . .":

The father continued to operate the assets for his own benefit, retaining all of the income for his own purposes and benefit, and without accounting to appellants. Appellants never at any time took part in the management of the business or businesses involved, never received accounts or statements, and were not even shown partnership returns or consulted with respect to their individual returns. The managing partner of S & P Company, the interest in which was the principal asset of the alleged partnership, was never informed that fifty per cent of S & P had been assigned to the purported partnership. Appellants were not consulted with reference to the disposition of the assets of the alleged partnership and their apparent disappearance. No books or records were created for the alleged partnership until after the years in question.

(c) " . . . their (the parties') statements . . .":

The Government placed strong reliance upon statements purportedly against interest made by Newton in 1949, and by Margaret in 1950, that they were at that time partners in Sherry Enterprises. Both, however, were relying upon the statements of their father and the fact that the agreement had been written up and signed by them; moreover,

as will be pointed out hereinafter, the existence of a partnership in 1949 or 1950 would not necessarily import the existence of the partnership in 1945 and 1946;

(d) ". . . the testimony of disinterested persons . . .":

The testimony of the disinterested witnesses, Herndon Hughes, Paul Kalmanovitz, and James Murray, shows clearly that the appellants were not consulted either before or after the partnership agreement was signed, did not participate in the business, did not receive accounts or statements, did not prepare or participate in the preparation of returns, received no income or profits, and, indeed, were entirely disregarded.

(e) ". . . the relationship of the parties . . .":

Nathan Sherry, the father, was clearly a dominant individual, so far as his children were concerned. Their practice was to sign whatever he put before them, as they trusted him implicitly, and did not question him; indeed, the evidence indicates that the father would have brooked no questioning from his children.

(f) ". . . their (the parties') respective abilities . . .":

The father, Nathan, was apparently a highly successful and aggressive business man, with a background of circulation work for daily newspapers, followed by the operation of bars, night clubs, and restaurants. The appellants had had no business experience of any kind prior to or during the years in question.

(g) ". . . their respective . . . capital contributions."

Aside from the purported gift set forth in the partnership agreement and gift tax return, the appellants made no contributions either of capital or services to the alleged

partnership, either prior to its inception or up to and including the years here in question. The $20,000.00 purportedly originating from their mother and held by Nathan Sherry for the benefit of Newton and Margaret was obviously a myth. No proof was adduced that such fund existed or was contributed to the partnership, nor is there any evidence which would indicate that the money received by Newton and Margaret from their grandmother's estate, in the amount of $500.00 each, ever found its way into the partnership.

(h) ". . . the actual control of income and the purpose for which it is used . . .":

The father completely controlled the income, and no part of it was ever distributed to the children.

(i) ". . . and any other facts throwing light on their true intent . . .":

There was no change in the children's circumstances. Both continued to work for wages or salaries commensurate with the work performed by them. The fact that Margaret, in later years, was given some stock of doubtful worth and two pieces of real property (at least one of which was encumbered by mortgage) by her father in no way indicates the *bona fide* existence of a partnership, but, rather, the father's continuing desire to make some provision for his daughter.

In its decision the Tax Court leans heavily upon the case of *Maletis v. United States* (9 C. A.), 200 F. 2d 97, and the cases therein cited, holding in effect that, when a taxpayer has created a form of business for tax purposes, and in fact such form is a sham or fictional, it is only the Commissioner who has the power to sustain or disregard the fiction.

While it is true that the appellants signed the original partnership agreement, the amendment thereto, individual income tax returns, and documents authorizing additional assessment of taxes for 1945 based on revised earnings of Sherry Enterprises, and it is true that each stated under oath to Government agents investigating their father that he or she was a partner at the time of the statement, these facts, standing alone, omit the very essence of this case, to wit, that neither the father nor the appellants intended to join together in the present conduct of the enterprise. The appellants' only desire was to please their father and to obey his orders and instructions. They did not expect to receive, nor did they receive, income or property as a result of the arrangement set up by their father; nor were they intentionally and reasoningly parties to the arrangement. They were not free agents, acting under their own volition, but were, rather, under the dominion and control of their father. They did not elect to act as partners.

The father's intentions are also clear. He did not intend a present partnership but, rather, that he would continue to receive and enjoy all of the income and dispose of the assets as he saw fit, tempered by a measure of protection for his children in the event of his death. The arrangement also served to divest his wife (stepmother of appellants) of one-half of her community interest in the assets involved.

It is undoubtedly true that the position of Nathan Sherry, if he were taxed with the entire income by the Commissioner, or, on the contrary, if he were frustrated by the Commissioner in attempting to disregard the partnership, would be indefensible under the holding of this Court in *United States v. Maletis, supra.* The children,

however, not being the moving parties in establishing the business form, are not so inhibited.

Attention should be directed to the case of *Sellers v. Commissioner* (9 C. A., 1955), 218 F. 2d 380, wherein this Court entertained an appeal from a decision of the Tax Court that the family partnership there involved lacked good faith and a business purpose and therefore did not constitute a partnership for the purposes of taxation. In that case neither of the two children, a son and a daughter, contributed particular services to the partnership. Both, in fact, were away during a large portion of the period involved, the son being in the armed service and the daughter married to an Air Force officer, and neither contributed any services to the management of the partnership. Their capital contribution had consisted of promissory notes, which were subsequently paid from the profits of the enterprise. The partnership was under the management of the father, who utilized the funds as he saw fit and paid only small amounts to the children. The father also paid the taxes on the children's purported share of the partnership earnings. This Court stated, at page 383:

> "There was no evidence that the children ever instructed their father or the responsible employee in the family partnership to invest their money as it was invested or in any other way. From all these circumstances the tax court could have inferred that the father controlled the distribution of funds to the children and use of those funds.
>
> "From a consideration of all these factors it is apparent that the tax court was justified in concluding that the children were not bona fide members of this family partnership and that it was not attempted to be formed in good faith and for a business purpose. *To have decided otherwise would have been to violate*

> *the first principle of income taxation: that income must be taxed to him who earns it.* Commissioner of Internal Revenue v. Culbertson, supra; Lucas v. Earl, 281 U. S. 111, 50 S. Ct. 241, 74 L. Ed. 731." (Emphasis added.)

It is the contention of these appellants that, in the instant case, from the evidence before it, the Tax Court should have concluded that the children were not *bona fide* members of the family partnership and that "it was not attempted to be formed in good faith and for a business purpose," and that the Tax Court's decision to the contrary was violative of the principle that income must be taxed to him who earns it.

The effect of the Tax Court's decision, if permitted to stand, is to throw upon these two young persons tax deficiencies of approximately $75,000.00 each, including accrued interest, with presently accruing interest in excess of $3,000.00 per year. A lifetime of savings, in their current positions, would not meet these liabilities; indeed, it is doubtful if either could meet the annual interest requirement. This result would, indeed, be the visitation upon the children of the sins of their father.

Conclusion.

It is respectfully submitted that the decisions appealed from should be reversed.

Charles H. Carr,

Attorney for Appellants.

No. 16,109

In the United States Court of Appeals
for the Ninth Circuit

LILLIAN FERGUSON, NEWTON IVAN SHERRY
and LOIS SHERRY, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

On Petition for Review of the Decisions of the
Tax Court of the United States

BRIEF FOR THE RESPONDENT

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In the United States Court of Appeals
for the Ninth Circuit

No. 16,109

MARGARET LILLIAN FERGUSON, NEWTON IVAN SHERRY and LOIS SHERRY, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

On Petition for Review of the Decisions of the Tax Court of the United States

---

BRIEF FOR THE RESPONDENT

OPINION BELOW

The opinion of the Tax Court (R. 49-61) is not officially reported.

JURISDICTION

This appeal involves individual income tax deficiencies in the amount of $101,341.78, determined against petitioners for their calendar years, 1945 and 1946, as follows (R. 61, 62):

	1945	1946	Total
Margaret Lillian Ferguson [1]	$ 5,124.55	$45,333.52	$ 50,458.07
Newton Ivan Sherry [1] and Lois Sherry	5,123.17	45,760.54	50,883.71
	$10,247.72	$91,094.06	$101,341.78

Notice of the deficiencies was mailed to the taxpayers on October 28, 1954. (R. 9-17, 30-36.) On January 24, 1955, within the permitted ninety-day period, the taxpayers filed petitions for review with the Tax Court for a redetermination of the deficiencies under the provisions of Section 272 of the Internal Revenue Code of 1939. (R. 5-17, 26-36.) The Commissioner filed answers (R. 17-23, 37-43); the taxpayers filed replies (R. 24-25, 43-45); and a hearing was held on April 15, 1957 (R. 66-196). The decisions of the Tax Court, sustaining the income tax deficiencies for calendar years 1945 and 1946, were entered on May 19, 1958.) (R. 61, 62.) Petition for review by this Court was timely filed on June 16, 1958. (R. 63-65.) Jurisdiction is conferred on this Court by Section 7482 of the Internal Revenue Code of 1954.

QUESTION PRESENTED

Did the Tax Court err in finding and concluding, under the entire record, that the taxpayers, Newton

[1] Margaret Lillian Ferguson and Newton Ivan Sherry will hereafter sometimes be called the taxpayers. Lois Sherry's only interest is derived by reason of the fact that, as Newton's wife, she joined with him in filing joint income tax returns for the years in issue.

Sherry and Margaret Ferguson (a brother and sister), were partners in Sherry Enterprises, a family partnership, during its fiscal years ended June 30, 1945, and 1946, so as to be liable for income tax deficiencies assessed for their respective calendar years, 1945 and 1946 ?

STATUTES AND REGULATIONS INVOLVED

Internal Revenue Code of 1939:

SEC. 11. NORMAL TAX ON INDIVIDUALS.

There shall be levied, collected, and paid for each taxable year upon the net income of every individual * * * tax * * * .

(26 U.S.C. 1952 ed., Sec. 11.)

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * *

(26 U.S.C. 1952 ed., Sec. 22.)

SEC. 181. PARTNERSHIP NOT TAXABLE.

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.

(26 U.S.C. 1952 ed., Sec. 181.)

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b).

(26 U.S.C. 1952 ed., Sec. 182.)

SEC. 3797. DEFINITIONS.

(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—

* * * *

(2) *Partnership and partner.*—The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation; and the term "partner" includes a member in such a syndicate, group, pool, joint venture, or organization.

* * * *

(26 U.S.C. 1952 ed., Sec. 3797.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

> Sec. 29.22 (a)-1. *What included in gross income.*—Gross income includes in general compensation for personal and professional services, business income, profits from sales of and dealings in property, interest, rent, dividends, and gains, profits, and income derived from any source whatever, unless exempt from tax by law. (See sections 22(b) and 116.) In general, income is the gain derived from capital, from labor, or from both combined, * * * .

* * * *

STATEMENT

The pertinent facts, as stipulated (R. 46-49) and found by the court (R. 50-58), appear, as follows:

The taxpayers Newton Ivan Sherry and Margaret Lillian Ferguson are the children of Nathan Sherry. Nathan's first wife, the mother of Newton and Margaret, died in 1937. In 1938 Nathan married Lucille Lawler Sherry. Nathan died in 1954. Lois Sherry is the wife of Newton, and, aside from the fact that she filed joint returns with Newton, has no connection with the issue here involved. (R. 50.)

The taxpayers' returns for the calendar years 1945 and 1946 were filed with the Collector of Internal Revenue for the Sixth District of California. (R. 51.)

Nathan, after discussions with his lawyer and his accountants, had his lawyer draft a partnership agreement dated October 1, 1943 (R. 48), which stated in part (R. 51-52):

Whereas, First Parties [Nathan and Lucille] were married on the first day of April, 1938 and ever since said date have been and now are husband and wife; and

Whereas, since said marriage First Parties have acquired and now own and hold the hereinafter described properties as community property; and

Whereas, First Parties acquired all of said properties by and through their joint and several personal services actually rendered since the date of said marriage; and

That said properties are described as follows:

50% interest of S & P Company valued at $30,000.00;

25% interest of Hollywood Recreation Company valued at $25,000.00;

100% interest of Hollyway Cafe valued at $5,000.00;

50% interest of Monticello Cafe valued at $4,500.00;

33⅓% interest of Pago Cafe valued at $3,000.00;

12½% interest of Swing Club valued at $1,500.00; and

Whereas, Second Parties are the children of Nathan Sherry by a former marriage, and there are no children the issue of said marriage of First Parties. and

Whereas, First Parties desire to give and transfer to Second Parties one-half of their interest in the aforedescribed properties for the purpose of creating a partnership between and including all and every of parties hereto,

Now, Therefore, Be It Known By These Presents:

> That the parties hereto will become and remain partners for a term of one year if each and all of them shall so long live, and for and during such additional time as each and all shall so desire;
>
> * * * *

The S & P Company (hereinafter referred to as "S & P") owned and operated bars and restaurants. Paul Kalmanovitz owned the remaining 50 per cent interest in S & P. (R. 52.)

The partnership agreement, along with a letter requesting their signatures, was mailed to Newton, who was then on Guadalcanal as a member of the United States Marines, and to Margaret who was then stationed in Ohio as a member of the United States Navy. They, in turn, signed the agreement and mailed it back to their father who was in Los Angeles. At the time they signed the agreement Newton was twenty-three and Margaret was twenty. (R. 52.)

Nathan and Lucille filed gift tax returns dated March 15, 1944 (R. 48-49), for the year 1943 on which they each reported gifts of one-half the property transferred to the new firm. Margaret signed donee returns dated March 15, 1944, in connection therewith. Nathan signed donee returns as attorney in fact for Newton. (R. 52-53.)

The parties to the original agreement signed an amendment thereto (R. 48) dated July 1, 1944. This amendment stated that the firm's losses were to be borne in equal shares by the parties to the agreement. The amendment indicates that the firm was named

Sherry Enterprises (hereinafter referred to as "Enterprises"). (R. 53.)

Newton was on active duty with the Marines from January 1940 until May 1945. He returned to the United States in March 1945, and was in a hospital in Philadelphia, Pennsylvania, from then until May 1945. Margaret was on active duty with the Navy from February 1943 until November 1945. (R. 53.)

Throughout the period relevant to this proceeding Nathan possessed a power of attorney to act in behalf of Newton and Margaret. (R. 53.)

Partnership returns (R. 48) for Enterprises for fiscal years beginning July 1, 1944, and ending June 30, 1945, and beginning July 1, 1945, and ending June 30, 1946, dated September 13, 1945, and September 3, 1946, respectively, were signed by Nathan. The taxpayers did not examine, sign or have anything to do with the preparation of these returns. Their preparation and filing were carried out under Nathan's direction. (R. 53.)

At Nathan's direction accountants prepared the individual returns of Newton (R. 48) and Margaret (Respondent's Ex. A and B, Stip., par. 5, R. 48) for the calendar years 1945 and 1946. These returns disclosed that Newton and Margaret each had $21,599.28 of income from Enterprises in 1945 and $19,156.85 in 1946. The taxpayers signed their respective 1945 returns on March 13, 1946. The returns for 1946, signed by the taxpayers, were received in the office of the Collector of Internal Revenue on March 15, 1947. Nathan saw to the preparation and filing of these returns and also arranged for the pay-

ment of the tax shown to be owing on the returns. (R. 53-54.)

Newton enrolled in college for the fall semester of 1945, but dropped out before completion of the semester in order to work for S & P. This was done in response to directions from Nathan. Newton was employed by S & P as manager of a drive-in and bar known as the Bayview Club. His salary was $110 per week. This job ended sometime in 1946. At no time during this employment did Newton have anything to do with the keeping of the books and records of the Bayview Club. (R. 54.)

In 1946 Newton purchased a home for $8,599. The money for this purchase was given to him by his father. The house was sold later in that same year and the money was returned to Nathan. Newton always considered that the house belonged to Enterprises. (R. 54.)

Margaret attended college during the spring semester of 1946. In the fall of that year she worked as an office girl in a perfume business named Sherry Dunn. Margaret believed that this business was owned by Enterprises. (R. 54.)

At Nathan's request Margaret sometimes made deposits and withdrawals for him at various banks. At some of these banks the accounts were in the joint names of Margaret and Nathan. During the period in which Margaret lived in her father's home she drew on these accounts to meet their household expenses. Margaret was married in March 1947 and ceased to live in her father's home. (R. 54-55.)

At the time of their mother's death and in the years following, Newton and Margaret were under the impression that their mother had left them $20,000 in the care of their father. It was their belief that Nathan used this money in his business, and that it was part of the capital of Enterprises. (R. 55.)

Sometime after their discharge from the Armed Forces Newton and Margaret each received approximately $500 as a result of the death of a grandparent. They turned this money over to Nathan to be used in Enterprises. (R. 55.)

In 1945 real property valued at approximately $52,500 was placed in Margaret's name. In 1946 real property valued at approximately $2,500 was also placed in her name. All of this property was placed in her name at Nathan's direction. Margaret did not consider herself the owner of this property. She thought it belonged to Enterprises. (R. 55.)

In 1947 Nathan transferred stock in the Marguery Corporation, which operates Lucy's restaurant, to Margaret. Nathan had purchased this business with funds from Enterprises. Margaret, at the time of the transfer from her father, considered herself the owner of the transferred shares. For a time Margaret was president of the corporation; at the time of the trial she managed the restaurant and owned 20 per cent of the corporation's outstanding stock. (R. 55-56.)

Margaret is the record owner of a "fourplex" apartment house valued at approximately $14,000. Her rights in this property were transferred to her

by her father. It was subject to an existing attorney's lien, and there is now an outstanding "assignment" of her rights in this property. (R. 56.)

Margaret is the owner of a "triplex" apartment house valued at approximately $35,000. This house belonged to Enterprises prior to its transfer to Margaret in 1950. Since the transfer of the "triplex" Margaret has made all the mortgage payments thereon. (R. 56.)

Newton and his wife signed a "Waiver of Restrictions on the Assessment and Collection of Deficiency in Tax (Form 870) dated July 19, 1948, for the year 1945 (R. 100, 196), for the amount of $1,114.42. (See Stip. par. 4, R. 47-48.) The address under their signatures is 5444 Melrose Avenue, Los Angeles. Lucy's Restaurant is located at that address. In a letter dated September 9, 1948, mailed to the Melrose Avenue address, the Commissioner indicated that the deficiency was caused by an increase in Newton's distributive share of Enterprises' income. (R. 56.)

On November 2, 1949, in the course of the Internal Revenue Service's investigation of Nathan's income, Newton testified under oath (Stip. by Counsel, R. 102, 185, 186) that he was then a partner in Enterprises. (R. 56.)

Margaret signed a "Waiver of Restrictions on Assessment and Collection of Deficiency in Tax" (R. 139, 196), dated July 1948, for the year 1945 for the amount of $1,109.75. The address under Margaret's signature was 5444 Melrose Avenue, Los Angeles. In a letter dated September 9, 1948, mailed to the Melrose Avenue address, the Commissioner

indicated that the deficiency was caused by an increase in Margaret's distributive share of Enterprises' income. (R. 56-57.)

On May 15, 1950, in the course of the Internal Revenue Service's investigation of Nathan's income, Margaret testified under oath (R. 141, 142) that she was then a partner in Enterprises. (R. 57.)

In 1947 S & P was dissolved. Neither Newton nor Margaret had any connection with the negotiations leading to a division of that company's property. (R. 57.)

One of the former S & P properties not taken by Paul Kalmanovitz upon dissolution of that company was the Clover Club and its underlying real property. This property was placed in a trust the beneficiaries of which were Newton and Margaret. The trustee of this trust was an accountant employed by Nathan. The Clover Club was later destroyed by fire. Subsequently this property was sold. Nathan received the proceeds of the sale. The trustee did nothing to protect the interests of the beneficiaries. Nathan was in control of Enterprises; however, at various times he, his wife, Newton and Margaret held informal meetings at which Enterprises' business was discussed. (R. 57.)

The earliest that Paul Kalmanovitz heard of the existence of Enterprises was 1947. (R. 57.)

Newton and Margaret never asked to examine, or examined any of the books or records of Enterprises or of S & P. Nor did they ever request an accounting in connection with either of these firms. (R. 58.)

The Commissioner increased the income of Sherry

Enterprises for the years relevant to the taxpayers' taxable years 1945 and 1946, and accordingly increased their distributive shares and their income taxes for those years. (R. 58.)

The taxpayers Newton and Margaret were partners in Sherry Enterprises during the years in question. (R. 58.)

SUMMARY OF ARGUMENT

The Tax Court correctly found and concluded, under this entire record, that Newton Sherry, the son of Nathan Sherry, deceased, and Margaret Ferguson, the daughter, were partners of Sherry Enterprises, a family partnership, during the taxable years 1945 and 1946.

Unlike the familiar family partnership federal tax controversy wherein the taxpayer is endeavoring to establish validity of the business organization form in question, this case presents the *reverse issue* of an existing partnership, organized and held out as valid by the taxpayers and other family members, throughout the taxable period, but now disavowed and claimed by them to have never possessed validity. In such circumstances, the controlling legal principles are well settled that: (a) the Commissioner can elect to rely on the validity of the family partnership organizational form which the taxpayers have themselves created; and (b) the burden is on the taxpayers, who are disavowing the existence of their own partnership, to prove that no valid family partnership ever existed. Under the agreed facts here obtaining, the Tax Court had more than ample justi-

fication for finding and concluding that these taxpayers failed completely to sustain their burden. Such a finding is, of course, entitled to finality where, as here, it is supported by substantial evidence and is not shown by the taxpayers to be clearly erroneous.

No question here exists as to the formation of the partnership on October 1, 1943, and as to its operation throughout and during the taxable years 1945 and 1946. At the time of formation both Newton and Margaret were on active duty in the armed forces. However, both admitted they signed the partnership agreement and executed an amendment thereto, dated July 1, 1944. Margaret admitted that, as donee, she signed the gift tax returns executed by her father and step-mother. Both admitted signing individual income tax returns for 1945 and 1946, reporting their respective shares of partnership income, as reflected on Sherry Enterprises' information returns for its fiscal years ended June 30, 1945, and 1946. Finally, both admitted signing waivers on restrictions on the assessment and collection of deficiencies in tax with respect to their 1945 income tax returns.

Over and beyond the above-described admitted formal partnership acts, Newton's and Margaret's testimony, far from being such as to sustain their burden of proving invalidity, was, at best, self-contradictory. Both taxpayers were confronted with their prior sworn testimony given in connection with their deceased father's 1949 income tax investigation, in which they had stated, under oath, that they were actively participating partners in Sherry Enterprises.

On the precise issue of bona fides which they here deny, Newton's testimony was expressly impeached by his prior sworn statement, in three particulars, and Margaret admitted, on cross-examination that she did not believe the partnership to be a sham tax avoidance scheme; that she did consider it to be a bona fide genuine partnership; and that she considered herself to be a bona fide partner. Furthermore, both children's denials that they performed vital services, contributed capital, or received distributions amounted, at most, to inconclusive self-serving assertions in the light of the record. The Tax Court pointed out that the family partnership's functions as a holding company minimized the performance of services as a key attribute of family partnership status; both Newton's and Margaret's testimony indicated that both may well have contributed inherited capital to the partnership; and both admitted partnership funds had been employed in establishing businesses in which they had variously worked. Margaret admitted her present ownership of certain rental and residential properties which had either formerly belonged to the partnership or possibly been acquired with its funds.

In the context of the case, the admissions contained in the record testimony—coupled with the repeated express acknowledgements of formal partnership organization and operation—more than amply support the Tax Court's conclusion that the taxpayers have here failed to sustain their burden of proving that they were not partners in Sherry Enterprises during

their taxable years, 1945 and 1946. The record sustains the fact finding that they were partners.

ARGUMENT

Under This Entire Record, the Tax Court Correctly Found and Concluded That the Taxpayers Were Partners, for Federal Tax Purposes, In a Valid Family Partnership

The Tax Court correctly found (R. 58) and concluded (R. 60) that, under the entire record, Newton Sherry, the son of Nathan Sherry, deceased, and Margaret Ferguson, the daughter, were partners of Sherry Enterprises, a family partnership, during the taxable years, 1945 and 1946, here involved.[2] This finding is entitled to finality where, as here, it is supported by substantial evidence and is not shown by the taxpayer to be clearly erroneous. *United States* v. *Gypsum Co.*, 333 U.S. 364, 395, rehearing denied, 333 U.S. 869; Section 7482(a) of the Internal Revenue Code of 1954; Rule 52(a) of the Federal Rules of Civil Procedure.

This case does not present the familiar family partnership federal tax issue wherein the burden rests on the taxpayer to show that "considering all the facts * * * the parties in good faith and acting

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[2] The deficiencies here in issue were assessed against the taxpayers, Newton (who filed joint returns with his wife, Lois Sherry) and Margaret, for their respective calendar years, 1945 and 1946. The additional income, so assessed, represents each taxpayer's additional distributive share of the income of Sherry Enterprises, the partnership, for its fiscal years ended June 30, 1945, and 1946. The amounts of each additional partnership income, as computed by the Commissioner, were not contested. (Stip. par. 2, R. 47.)

with a business purpose intended to join together in the present conduct of the enterprise." *Commissioner* v. *Culbertson*, 337 U.S. 733, 742. Instead, as the Tax Court pointed out (R. 58, 60), it presents the *reverse situation*, namely: present an existing partnership, organized and held out as valid by the taxpayers and other family-members throughout the taxable period, "here it is the partners who have assumed the burden of repudiating their own partnership." *Sherman* v. *United States*, 141 F. Supp. 369, 370 (E.D. Pa.), affirmed *per curiam*, 240 F. 2d 600 (C.A. 3d).

Moreover, the taxpayer-family members' contention that the formal business unit they themselves created cannot constitute a valid family partnership, for tax purposes, becomes irrelevant, and must yield to the practical administrative exigencies, which permit the Commissioner in such circumstances, to take the taxpayer at his word and sustain the representations which the taxpayer himself made to the taxing authorities. *Maletis* v. *United States*, 200 F. 2d 97 (C.A. 9th), certiorari denied, 345 U.S. 924; *Phillips* v. *United States*, 193 F. 2d 132 (C.A. 5th). See also *Higgins* v. *Smith*, 308 U.S. 473, 477; *Moline Properties* v. *Commissioner*, 319 U.S. 436; *Love* v. *United States*, 96 F. Supp. 919, 921 (C. Cls.). As former Chief Judge Denman stated in the *Maletis* case (p. 98):

> The Bureau of Internal Revenue, with the tremendous load it carries, must necessarily rely in the vast majority of cases on what the taxpayer asserts to be fact. The burden is on the

> taxpayer to see to it that the form of business he has created for tax purposes, and has asserted in his returns to be valid, is in fact not a sham or unreal. If in fact it is unreal, then it is not he but the Commissioner who should have the sole power to sustain or disregard the effect of the fiction since otherwise the opportunities for manipulation of taxes are practically unchecked. That which best serves the purpose of the tax statute should govern in this field and not the yearly exigencies of this taxpayer. * * *
>
> Taxpayer argues that in fact he could have no election since what he created could never constitute a valid family partnership for income tax purposes. That what he created cannot be a valid family partnership for tax purposes is irrelevant, since he elected to do business as a partnership and represented it to be valid. He elected the form and arrangement in which he would do business. Having adopted that form, even though his actions were so inadequate as to make the form unreal for income tax purposes, "The Government may look at actualities and upon determination that the form employed * * * is unreal * * * may sustain or disregard the effect of the fiction as best serves the purposes of the tax statute." *Higgins* v. *Smith, supra.*

We submit the above cited authorities amply support the correctness of the Tax Court's conclusion below (R. 58, 60):

> Here, petitioners seek to disavow the existence of the partnership. The burden of proof is upon them, and we cannot find on this record that it has been carried.
>
> * * * *

> Perhaps, if the burden of proof were on the Government, we would hold in favor of petitioners. But the burden is not upon the Government; it is upon petitioners, and we cannot find from the evidence presented that they were not in fact partners in Sherry Enterprises during the tax years. Accordingly, we have found as a fact that they were partners during the years in controversy.

Cumulatively, the record furnishes, *inter alia*, the following evidentiary support for taxation of these taxpayers as partners in Sherry Enterprises: (1) Taxpayers agree that, on October 1, 1943, the partnership agreement (R. 51-52), giving rise to their respective taxable distributive shares (25 per cent to Newton and 25 per cent to Margaret) was duly executed (Ex. G, Stip. par. 8, R. 48). Newton admitted signing the agreement (R. 86, 92-93) and so did Margaret (R. 110). (2) Taxpayers agree that Nathan and Lucille Sherry, on March 15, 1944, filed gift tax returns for the year, 1943, on which they each reported gifts of one-half of the property transferred to Sherry Enterprises, the partnership. (R. 48-49.) Taxpayers' witness, accountant Herndon Hughes, who prepared the gift tax returns (R. 68-69), admitted on cross-examination, that, at the time of preparation, he believed Sherry Enterprises to be a bona fide partnership (R. 80-81). Newton was not interrogated further about his participation in the transaction. Margaret admitted her signature, as donee, on the gift tax returns (R. 113-114, 124) and her belief that it was not a sham (R. 128). (3)

Taxpayers agree that they signed an amendment (R. 53) to the original partnership agreement, which was dated July 1, 1944, and provided that the firm losses would be borne equally by the parties to the original agreement (R. 48). (4) Taxpayers agree that Sherry Enterprises filed information returns (R. 48) for its fiscal years ended June 30, 1945, and 1946, and that both Newton and Margaret filed individual income tax returns for their calendar years 1945 and 1946 (R. 48), on which returns each reported income of $21,599.28 from the partnership, for 1945, and $19,156.85, for 1946 (R. 53-54). Newton admitted signing his joint return (filed with his wife, Lois) for 1945 (R. 88), and also stated his belief that he signed the return for 1946 (R. 88). Margaret admitted her signature on both of her returns. (R. 114, 116-117, 153.) (5) Both Newton and Margaret admitted their respective signatures on waivers of restrictions on the assessment and collection of deficiencies in tax with respect to their 1945 income tax returns based upon increases in their respective distributive shares of Enterprises' income. (R. 56-57, 59, 100-101, 139-140, 196.) Newton's signed waiver was dated July 19, 1948, and related to an additional assessment of $1,114. (R. 100, 101.) Margaret's waiver, dated September 9, 1948, related to a deficiency assessment of $1,109.75. (R. 139.)

Obviously, the above-detailed and admitted formal acts, performed by taxpayers, evidence the fact that Sherry Enterprises was held out to the Commissioner —agreement-wise, gift tax-wise, and income tax-wise —as a business partnership. Since the family mem-

bers' election to organize as a partnership and to distribute income to named partners during the taxable period was formally subscribed to by the taxpayers themselves, it is clear that, for federal tax purposes, irrespective of the reality and validity of the business form selected, the Commissioner was here entitled to hold the taxpayers to the tax liability attaching to the business unit of their choice. *Maletis* v. *United States, supra; Phillips* v. *United States, supra; Higgins* v. *Smith, supra.* However, the record furnishes additionally compelling support for the correctness of the Tax Court's finding and conclusion.

Faced with the burden of having to prove invalidity of the partnership, the taxpayers attempted to deny: (a) knowledge of the import of their formal partnership actions taken; (b) performance of any significant services to the partnership (R. 59); (c) failure to receive substantial distributions (R. 59-60); and (d) absence of substantial capital contributions. For example, Newton testified, *inter alia*, that: (a) he did not read the partnership agreement (R. 87); did not remember signing any returns for the partnership (R. 87); did not look at the returns he signed (R. 94); never considered himself to be a partner (R. 100); and indicated he depended on his father's instructions as to execution of all pertinent documents (R. 96); (b) he never discussed business with his father (R. 98); and never attended family meetings at which business policies and plans were discussed (R. 98); and only did what his father told him, no matter what it was (R. 108); (c) he never

received any funds from Sherry Enterprises and did not to his knowledge, pay any taxes on income from it (R. 89); and (d) he never personally had any money of his own to invest in the partnership (R. 106).

Considering the burden Newton was attempting to carry by his above-indicated "broad denials" (R. 60), the record does clearly indicate his utter failure to satisfy such burden. The plea of ignorance of the import of his partnership acts, formally performed, does not, of course, absolve him from partnership liability, in any event, but, at best, it is merely self-serving. The Tax Court based its conclusion, in part, upon his conviction that the taxpayers had not (R. 60) "satisfactorily explained away the obvious conclusions to be drawn from these facts" (*viz.*, the formally executed partnership acts, described above). Upon review, due regard should properly be accorded the opportunity afforded the trial court to view the witnesses and judge their credibility. *Quock Ting* v. *United States*, 140 U.S. 417; *United States* v. *Gypsum Co.*, 333 U.S. 364, 395, rehearing denied, 333 U.S. 869; *National Brass Works* v. *Commissioner*, 205 F. 2d 104 (C.A. 9th); *Ferrando* v. *United States*, 245 F. 2d 582 (C.A. 9th). Moreover, here, the record shows, as will be developed, *infra*, that, with respect to at least three material avowments, Newton's credibility was impeached.

As to performance of services, the record shows that, after his discharge from the Marine Corps, Newton worked for a time (R. 90-91, 95-96) as

manager of the Bayview drive-in and bar, at Wilmington, California. The establishment was one of the S & P partnership properties, 50 per cent of which constituted an important component of Nathan's ownership interest contributed as underlying assets of Sherry Enterpries. (R. 51, 90.) For purposes of sustaining the taxpayers' burden of proof, the significance, or insignificance, of the services rendered is in all events, inconclusive. As the Tax Court pointed out (R. 59), the fact that either taxpayer, here, might not have rendered significant services to Sherry Enterprises "is not surprising since it was in the nature of a holding company." (See Witness Hughes' testimony, R. 74-75.) Furthermore, Newton's express denials that: he never considered himself a partner of Sherry Enterprises (R. 98); and never attended meetings and discussed policies and plans of the partnership (R. 98) were specifically impeached and contradicted by his prior sworn testimony given to Special Agent Burns of the Intelligence Division, Internal Revenue Service (R. 184), on November 2, 1949, in connection with the tax investigation of his father, Nathan Sherry. At that time he stated, under oath, that he was a partner (R. 102-103) and, with respect to partnership policy formulation, that he did participate in deliberations "if ever we wanted any type of business whatsoever added to the Sherry Enterprises" (R. 107).

With respect to partnership distributions, the record shows (R. 98-100) that Newton purchased a home for $8,599 in 1946 with Sherry Enterprises' funds and that, subsequent to the taxable period, he

worked at Linda Gale, Inc., a business established for him with Sherry Enterprise funds (R. 99). Finally, with respect to capital contributions, Newton testified to his understanding (R. 105) that $20,000 left by his mother was invested in the family business. This understanding was confirmed by Margaret. (R. 128-129.) However, Newton's express denial (R. 106) that he never had any personal funds of his own to invest in the partnership was impeached and contradicted by his prior sworn testimony of November 2, 1949 (R. 106-107), wherein he stated: "Also, there was money that was left to us that made up the partnership. Also, there was money I invested that made up the partnership."

Following the same broad denial pattern as her brother, Margaret's record testimony similarly evidences a telling failure to satisfy the taxpayers' assumed burden of proof. With respect to each of the above-indicated categories of denial, Margaret testified, *inter alia*, that: (a) she did not recall reading the partnership agreement, when she signed it (R. 111, 125, 127-128); she was not sure (contrary to the stipulation) that she signed the amendment thereto (R. 125-127); she looked at the figures on her tax returns, when she signed, but they did not mean anything (R. 114); she did not understand the significance of the waiver when she signed it (R. 140); she had no knowledge (with one minor exception, R. 147) of what became of the bars and restaurants that were 50 per cent owned by Sherry Enterprises, through S & P (R. 146-149); and she did not have "any feelings about being anything" when she was

returning her reported share of partnership income (R. 154); (b) as to services, she did not undertake to manage Sherry Enterprises and was not consulted (R. 111, 117, 119); her work performed consisted only of answering the telephone and taking messages (R. 130); she had nothing to do with setting business policies (R. 118); and there were no formal meetings to discuss policies, except, perhaps, occasionally at dinner (R. 118); (c) distributions-wise, she never received any income from Sherry Enterprises (R. 122); she never considered she owned any assets personally (R. 131); nothing was left in her father's estate when he died (R. 132, 145); and she never discussed with her brother the reasons why they were not receiving anything from the partnership (R. 151); and (d) as to capital contributions, she endorsed over to her father a $500 check received from her grandmother's estate (R. 119-120, 128); and she understood that $20,000, left to her brother and herself by her mother, was invested for them in the partnership (R. 128-129).

Whereas the foregoing self-serving attempts to deny partnership validity are, in themselves, much too indecisive and indefinite to sustain the burden of proof incumbent upon the taxpayers in this case, they become totally inadequate for such purpose when Margaret's self-contradictory testimony, which stands side by side with them in the record, is examined. For example, she also testified that: despite her protestations of lack of knowledge of the partnership (set forth above) she was aware of the partnership's existence when she signed the partnership agreement

(R. 113); she knew the gift tax return would be filed with the Government and felt, at the time of execution, that it was a true gift and not a sham (R. 128); she knew of no conversations with family members at the time of creation of the partnership which would indicate the partnership agreement was a sham or unreal (R. 155); she did not consider that the partnership was created as a tax avoidance scheme of her father's (R. 154); she considered the partnership to be bona fide and genuine at the time she entered into it (R. 155); during the taxable years under review, she felt she was a bona fide member of Sherry Enterprises (R. 132); and she signed a prior voluntary sworn statement, on May 15, 1940 (R. 141, 142), which contained admissions to the same effect (R. 141-142).

With respect to services performed, she had a joint bank account with her father on Sherry Enterprises' account, went to the bank and cashed checks and made deposits therein (R. 117-118); during 1946, she worked at Sherry Dunn, a perfume business in which the partnership owned an interest (R. 129-130); she was president and a 20 per cent stockholder of Marguery Corporation, which owned Lucy's Restaurant (where she worked) and whose stock she believed to have been purchased by her father with Sherry Enterprises' money (R. 134-135, 136, 143); there were informal meetings of the four partners, sometimes at social gatherings (R. 140); and she signed a prior sworn statement (R. 141, 142), in which she testified under oath in 1950 that she was then a partner in Enterprises (R. 57). Despite her

denial of partnership distributions, she drew checks on Sherry Enterprises' account to pay household expenses of herself and her father when she lived at home (R. 118); during the period under review real estate lots valued at $2,500 and a building valued at $52,500, both of which were Sherry Enterprises' assets, were transferred into her name (R. 130-131); she presently owned a fourplex apartment on North Irving Boulevard, which had formerly been her father's but title to which had been transferred to her, with the source of purchase money being unidentified (R. 136-137); and, in addition, she held title to a triplex apartment, on which she made mortgage payments, but which, at one time, was an asset of Sherry Enterprises (R. 137-138).

Again, with respect to capital contributions, the gift (from her father and step-mother) of her partnership interest was, admittedly, real and genuine (R. 128); she "knew" the $20,000 bequest from her mother "had been left for my brother and I" and understood it was contributed to Sherry Enterprises (R. 128-129); and she personally endorsed over her own $500 contribution to capital (R. 119-120, 128).

Because of the nature of Sherry Enterprises as a family holding company partnership carrying on no real operations of its own (R. 59, 74-75) and with the performance of services not constituting a dominant factor in its successful conduct during the period (R. 59), the testimony of Witnesses Paul Balmanovitz (R. 157-163) and James F. Murray (R. 164-183) added little or nothing to taxpayers' futile attempt to sustain their burden of proof with respect to the

partnership's alleged invalidity. It is entirely irrelevant that Kalmanovitz, as the so-called managing partner (R. 159-163) of S & P, the principal operating partnership, knew nothing of the existence of Sherry Enterprises until the time of the criminal trial of Nathan Sherry, in 1952 (R. 159). It is equally irrelevant that Kalmanovitz' dealings with the Sherry family were almost entirely with Nathan Sherry (R. 158-159, 161), since it is perfectly consistent with the finding of a family partnership (R. 58) that one principal partner should act in a representative capacity for the group, and particularly so, when the partnership is not an operating company, but in the nature of a holding company. As for Murray's testimony, his direct testimony (R. 164-174) reaffirms (R. 164) the fact of the family partnership's organization and existence throughout the taxable period and his testimony on cross-examination (R. 174-181) cumulatively strengthens the claim of its validity since he admitted (R. 175-176) that he had no reason to believe and would not say that Sherry Enterprises was a fictitious partnership. The principal purpose of Government Witness Burns' testimony (R. 184-196) was to lay a foundation for the introduction of the prior sworn contradictory testimony of both taxpayers in connection with the investigation of their father, Nathan Sherry, which testimony was given in 1949 and 1950. It is also to be observed that Burns recommended, on the basis of his examination of the case, that the partnership should be recognized, consistent with the taxpayer's own contentions. (R. 193-194.)

We submit that the foregoing analysis of the record clearly shows that the taxpayers have failed utterly to carry their burden of proving the invalidity of Sherry Enterprises as a family partnership, for federal tax purposes. We submit further that the entire record furnishes more than ample support for the Tax Court's finding that Newton and Margaret were partners in Sherry Enterprises during the years in question. Manifestly, the Tax Court's finding (R. 58, 60) can in no proper view be regarded by a reviewing court as clearly erroneous.

The argument contained in taxpayers' brief (R. 13-19) constitutes a studied refusal to acknowledge both the *reverse* family partnership setting in which the issue of invalidity arises and the resulting burden, which is theirs, of having to prove, by a preponderance of the evidence, such invalidity. As we have already shown, this they have failed utterly to do. Moreover, in such circumstances, the taxpayers' reliance (Br. 13-16) on *Commissioner* v. *Culbertson*, *supra*, and on this Court's decision (Br. 18-19) in *Sellers* v. *Commissioner*, 218 F. 2d 380, is of no help to them. Finally, their attempt (Br. 17-18) to avoid the impact of *Maletis* v. *United States*, *supra*, on the grounds that the father, Nathan Sherry (rather than themselves), was the moving party in organizing the partnership, is, at most, a distinction without a difference. See *Sherman* v. *United States*, *supra*.

CONCLUSION

The decision of the Tax Court should be affirmed.

Respectfully submitted,

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No. 16,109

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

MARGARET LILLIAN FERGUSON, NEWTON IVAN SHERRY and LOIS SHERRY,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

APPELLANTS' REPLY BRIEF.

FILE
DEC 11 1958
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FOR THE NINTH CIRCUIT

MARGARET LILLIAN FERGUSON, NEWTON IVAN SHERRY and LOIS SHERRY,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

APPELLANTS' REPLY BRIEF.

It is, of course, not disputed that the situation presented in the instant appeal is the reverse of that ordinarily found in cases involving so-called family partnerships. Ordinarily, the Commissioner of Internal Revenue is on the side attacking the validity of the partnership and attempting to lay the tax burden upon the shoulders of a single one of the alleged partners.

Despite this shift from his ordinary position in such matters, the same rules of law apply in the determination of the controversy between the adversaries as would apply if the Commissioner were on the opposite side thereof.

It is the contention of these appellants that the Commissioner, in his original determination, and the Tax Court, in its decision, have overlooked or ignored certain basic principles of law and justice which require a result

other than that reached by the Tax Court and here put forward by the Respondent in his brief filed with this Court. It is appellants' contention that they were not members of a family partnership into which they had willingly or freely entered, and that the purported family partnership attempted to be set up by appellants' father was not formed in good faith or for a business purpose.

The Evidence.

Respondent, under the heading "Statement" (Resp. Br. 5-13), has merely restated the findings of fact by the Tax Court, rather than summarizing all of the evidence produced, as was done by the appellants in their opening brief (App. Br. 4-12). The effect, therefore, was merely to present a summary of those evidentiary matters and conclusions drawn by the trier, thus minimizing the overwhelming evidence contained in the record which indicated that the appellants were entirely passive participants in the scene, acting solely under the dominance of their father, and without hope or expectation of ultimate reward, other than the satisfaction of being dutiful and obedient children to their surviving parent. The idea of the so-called partnership was originated in their absence, the papers were drawn at the instructions and instance of their father, without their consultation, and the papers then sent to them with the command to sign. As pointed out in the opening brief, the appellants never participated in the partnership affairs, nor reaped any benefit therefrom. They obviously contributed nothing, either by way of capital or services, and received nothing by reason of their alleged "partnership."

This Court is clearly not bound by the alleged findings of fact as construed by the Tax Court and as propounded by respondent, but is entitled to view and search the en-

tire record of the proceedings and to relate every part of the substantial evidence to the whole of the evidence, and to draw such inferences or conclusions therefrom as this Court may deem proper, the inferences or conclusions of the Tax Court notwithstanding (*Gillette's Estate, et al. v. Commissioner* (C. A. 9, 1950), 182 F. 2d 1010; *United States v. United States Gypsum Co.,* 333 U. S. 364, 394-395; *Int. Rev. Code of 1954,* Sec. 7482(a); *Fed. Rules Civ. Proc.,* Rule 52(a)).

We therefore believe that this Court will look to the evidence as a whole, and not merely confine itself to those portions selected by the Tax Court and by the respondent to support his position.

Burden of Proof.

Respondent would seek to imply that, by reason of the fact that appellants herein are attacking a determination by the Commissioner that a partnership did in fact exist in 1945 and 1946, they have assumed some "burden of proof" over and beyond that which is required of taxpayers in any other appeal to the Tax Court from the Commissioner's determination (Resp. Br. 16-17, 29). We can find no support for this contention, either in the reported cases or in logic.

It is true that there is an initial presumption of correctness which attaches to any final determination by the Commissioner. This presumption, however, is one of law and not an inference of fact, and hence disappears when evidence sufficient to sustain a contrary finding has been introduced (*Crude Oil Corp. of America v. Commissioner* (C. A. 10, 1947), 161 F. 2d 809, and cases there collected; *Gillette's Estate v. Commissioner, supra; Lawrence v. Commissioner* (C. A. 9, 1944), 143 F. 2d 456).

Here, the evidence was not only sufficient to sustain a finding that the appellants had not entered into a partnership arrangement with their father, but, indeed, is compelling to the finding that they did not. The very primary essential to such a relationship, *a free and voluntary meeting of the minds, is entirely lacking.* Looking through the form (the documents signed by appellants under the domination of their father) to the substance (the control, management, and disposition of the property and its earnings) furnishes overwhelming evidence to refute the existence of an obligation which these children did not create and the fruits of which they never enjoyed (*cf. Gillette's Estate v. Commissioner, supra*).

Gist of Respondent's Argument.

The respondent, however, apparently does not place great reliance upon his repeated assertions that the appellants have failed to carry their "burden of proof," as he places the greatest weight (as did the Tax Court) upon the principles enunciated by this Court in *Maletis v. United States,* 200 F. 2d 97, cert. den. 345 U. S. 924 (Resp. Br. 17, 20-21). Thus, he argues that, in view of the formal subscription of the "partnership agreement" and tax returns purporting to show distribution of income, the appellants are precluded from attacking the reality and validity of the partnership, and the Commissioner's determination is unassailable.

Hence, argues the respondent, the appellants are not entitled to the benefit of the rules laid down by the Supreme Court in *Commissioner of Internal Revenue v. Culbertson,* 337 U. S. 733, 93 L. Ed. 1695, and by this Court in *Sellers v. Commissioner,* 218 F. 2d 380, for the determination of a valid and subsisting partnership for

purposes of taxation (*cf.* Resp. Br. 29), as contended by appellants in their opening brief.

In the *Maletis* case, the appellant was the *father,* who had created the purported partnership, elected to do business under that form, represented it in his returns to be a valid entity, and thereafter, because of a tax advantage to be gained, sought to disavow it. Under such circumstances, when the Commissioner, in the exigencies of tax collection, decided to hold the taxpayer to his original representations, the taxpayer could not be heard to complain, and the actual invalidity of the partnership was held to be irrelevant. Thus, in practical effect, the taxpayer, through his own active conduct and representations, had estopped himself from asserting the invalidity of that which he had created.

Undoubtedly, if the appellant here were Nathan Sherry, the father of these appellants, seeking to question the validity of the instant purported partnership, the principles of the *Maletis* case might apply. But these appellants, under the circumstances here disclosed by the evidence, are not so foreclosed. In reality, the acts and representations were not theirs, but those of their father. They should not be condemned to paying taxes upon income which they neither earned nor received. They clearly fall within the ruling of this Court enunciated in *Sellers v. Commissioner,* 218 F. 2d 380 (App. Br. 18-19).

Conclusion.

It is respectfully prayed that the decisions appealed from be reversed.

Charles H. Carr,

Attorney for Appellants.

No. 16110

United States
Court of Appeals
for the Ninth Circuit

JERRY LEE BIRDSONG and DENNIS BIRDSONG, by and through their guardian ad litem, Ora Mae Birdsong, and ORA MAE BIRDSONG, Appellants,

vs.

UNITED STATES OF AMERICA, Appellee.

Transcript of Record

Appeal from the United States District Court for the Northern District of California, Southern Division

FILED
OCT - 1 1958
PAUL P. O'BRIEN, CLERK

Phillips & Van Orden Co., Fourth and Berry Sts., San Francisco, Calif.—9-19-58

No. 16110

United States Court of Appeals

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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United States Attorney,

FREDERICK J. WOELFLEN, Esq.,
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San Francisco, California,

For Appellee.

In the United States District Court for the Northern District of California, Southern Division

No. 35390—Civil

JERRY LEE BIRDSONG and DENNIS BIRDSONG, by and through their guardian ad litem, ORA MAE BIRDSONG, and ORA MAE BIRDSONG, Plaintiffs,

vs.

UNITED STATES OF AMERICA, Defendant.

DOCKET ENTRIES

1956

Apr. 10—Filed complaint—issued summons.

Apr. 10—Filed petn. and order appointing Ora Mae Birdsong, gdn. ad litem of Jerry Lee Birdsong and Dennis Birdsong.

* * * * *

June 12—Filed notice and motion by deft. for more definite statement, June 25, 1956.

June 12—Filed memo. of deft. in support of motion for more definite statement.

June 25—Ordered, motion for more definite statement continued to July 2, 1956.

July 2—Ordered after hearing motion for more definite statement submitted. (Murphy)

July 23—Filed order granting motion of defendant for more definite stmt. (Murphy)

July 24—Mailed copies order to counsel.

Oct. 9—Filed amended complaint.

1956

Nov. 19—Filed notice of motion by deft. for more definite statement, Dec. 3, 1956.

Nov. 19—Filed defendants memo. of points and authorities in support of motion for more definite statement.

Dec. 3—Ordered after hearing, motion for more definite statement granted. (Hamlin)

Dec. 4—Filed order granting motion of deft. for more definite statement. (Hamlin)

1957

Apr. 18—Filed second amended complaint.

May 7—Filed answer to second amended complaint.

May 17—Filed interrogatories by defendant to plaintiff Ora Mae Birdsong.

1958

Apr. 16—Mailed notice of dismissal calendar April 23, 1958.

Apr. 23—Ordered dismissed for lack of prosecution, April 23, 1958. (Goodman)

June 2—Filed notice and motion by plaintiff to set aside dismissal, June 9, 1958.

June 2—Filed affidavit of Jeremiah F. O'Neill, Jr. in support of motion to set aside dismissal.

June 6—Ordered motion to set aside dismissal assigned to Judge Goodman for hearing June 11, 1958. (Harris)

June 11—Ordered after hearing, motion to vacate dismissal, denied. (Goodman)

June 13—Filed notice of Appeal by plaintiff.

June 13—Filed appeal bond in sum $250.00.

1958

June 13—Filed appellant's designation of record on appeal.

June 13—Mailed notices.

June 13—Filed answer of plaintiff to interrogs. by defendant.

June 13—Filed appellee's counter designation of record on appeal.

[Title of District Court and Cause.]

COMPLAINT FOR WRONGFUL DEATH

Plaintiffs complain of defendant that:

I.

Prior to the filing of the complaint herein plaintiff Ora Mae Birdsong was duly appointed the guardian ad litem of the plaintiffs Jerry Lee Birdsong and Dennis Birdsong;

II.

At all times mentioned herein relevant plaintiffs were and are residents of the County of Alameda, State of California, within the jurisdiction of the above entitled court; this action is brought pursuant to the "Federal Tort Claims Act";

III.

At all times mentioned herein relevant defendant United States of America operated and controlled that certain Veterans Hospital located in the City of Oakland, County of Alameda, State of California;

IV.

Plaintiffs Ora Mae Birdsong, Jerry Lee Birdsong and Dennis Birdsong are the sole heirs at law of Thomas William Birdsong, deceased;

V.

On or about the 8th day of March, 1954, Thomas William Birdsong, deceased, was admitted to said Veterans Hospital for the treatment of ulcers and hypertension;

VI.

At said time and place the defendant, United States of America, had employed in said hospital certain physicians, surgeons, nurses and hospital aids; said physicians, surgeons, nurses and hospital aids were at all times herein mentioned acting within the course and scope of their employment;

VII.

On or about the aforesaid date, Thomas William Birdsong, deceased, was accepted as a patient by said physicians, surgeons, nurses and hospital aids, and they and each of them undertook in their respective capacities to attend and cure the decedent;

VIII.

At said time and place, and thereafter until his death on April 11, 1954, said physicians, surgeons, nurses and hospital aids, who were then and there agents and employees of said defendant, United States of America, and who were acting within the course and scope of their employment, did not use

due and proper care or skill in examining and endeavoring to cure and treat the decedent of the aforesaid ailments; and further, that pursuant to said undertaking said defendant, United States of America, by and through its agents, treated said Thomas William Birdsong in a negligent and unskillful manner, including that certain operation performed on said decedent on March 10, 1954;

IX.

As a proximate result of defendant's negligent and unskillful examination and treatment of decedent as aforesaid, said Thomas William Birdsong languished and died on the 11th day of April, 1954;

X.

Decedent was an able bodied man, capable of, and he did financially support his wife and children, the plaintiffs herein;

XI.

By reason of the premises, plaintiffs were compelled to and they did secure the services of duly licensed morticians and funeral homes, to their damage in a presently undetermined amount, which plaintiffs pray leave to insert by amendment when the same is determined;

XII.

By reason of the premises plaintiffs were deprived of the care, comfort, support, society, love and affection of Thomas William Birdsong, deceased;

XIII.

By reason of the premises, plaintiffs have been generally damaged in the sum of One Hundred Fifty Thousand Dollars ($150,000.00).

Wherefore, plaintiffs pray judgment against defendant as follows:

1. General damages in the sum of $150,000.00;
2. Special damages as may be alleged;
3. Costs of suit; and
4. Any further meet relief.

KAISER & O'NEILL,
/s/ By JEREMIAH F. O'NEILL, JR.,
Attorneys for Plaintiffs

[Endorsed]: Filed April 10, 1956.

[Title of District Court and Cause.]

PETITION AND ORDER FOR APPOINTMENT OF GUARDIAN AD LITEM

To the Honorable the Superior Court of the State of California, in and for the County of Alameda:

The petition of Ora Mae Birdsong respectfully shows:

I.

That petitioner is a resident of the City of Oakland, County of Alameda, State of California, and is the mother of Jerry Lee Birdsong and Dennis Birdsong, who are minors of the ages of ten (10)

years and nine (9) years respectively; that said minors reside at 1228 - 103rd Avenue, Oakland, California, and said minors have no general or testamentary guardian.

II.

That said minors have a cause of action against defendant above named, upon which their best interests require that they bring an action in this Court for damages.

III.

That your petitioner is a competent and responsible person, qualified to act as the Guardian ad Litem of said minors in said action; that no previous application for an appointment of Guardian ad Litem in this action has been made.

Wherefore, petitioner prays that she be appointed Guardian ad Litem for said minors to prosecute their action in their behalf.

/s/ ORA MAE BIRDSONG,
Petitioner Ora Mae Birdsong

State of California,
County of Alameda—ss.

Ora Mae Birdsong, being first duly sworn, deposes and says: That she is the petitioner in the above entitled matter; that she has read the foregoing Petition and knows the contents thereof; that the same is true of her own knowledge, except as to matters therein stated upon information or

belief, and as to such matters that she believes it to be true.

/s/ ORA MAE BIRDSONG

Subscribed and sworn to before me this .... day of April, 1956.

[Seal] /s/ ROBERT A. KAISER,
Notary Public in and for the County of Alameda, State of California.

ORDER

Ora Mae Birdsong is hereby appointed Guardian ad Litem of Jerry Lee Birdsong and Dennis Birdsong, plaintiffs herein.

Dated: April 10, 1956.

/s/ O. D. HAMLIN,
Judge of the Superior Court

[Endorsed]: Filed April 10, 1956.

[Title of District Court and Cause.]

MOTION FOR A MORE DEFINITE STATEMENT

To: The plaintiffs above named, and to their attorneys, Kaiser & O'Neill, Easton Building, Oakland 12, California.

You and each of you Will Please Take Notice that on Monday, June 25, 1956, at the hour of 9:30 a.m. or as soon thereafter as counsel may be heard, the defendant United States of America will, in

the courtroom of the Master Calendar Judge of the above court, Post Office Building, Seventh and Mission Streets, San Francisco, California, move for a more definite statement of the allegations in plaintiffs' complaint, pursuant to the provisions of Rule 12(e) of the Federal Rules of Civil Procedure.

Said motion will be based upon all the records and papers on file herein, and the defendant's memorandum of points and authorities filed herewith.

Dated: June 11, 1956.

LLOYD H. BURKE,
United States Attorney
/s/ FREDERICK J. WOELFLEN,
Assistant United States Attorney

Notice of Mailing attached.

[Endorsed]: Filed June 12, 1956.

[Title of District Court and Cause.]

ORDER

This is a motion for a more definite statement under Rule 12 of the Federal Rules of Civil Procedure.

The complaint charges that "said physicians, surgeons, nurses and hospital aids, who were then and there agents and employees of said defendant, United States of America, and who were acting within the course and scope of their employment, did not use due and proper care or skill in examin-

ing and endeavoring to cure and treat the decedent of the aforesaid ailments; and further, that pursuant to said undertaking said defendant, United States of America, by and through its agents, treated said Thomas William Birdsong in a negligent and unskillful manner, including that certain operation performed on said decedent on March 10, 1954".

The defendant is entitled to more information than the allegation contained in the above quoted paragraph in order to prepare his defense.

The motion for a more definite statement is granted.

Dated: July 23rd, 1956.

/s/ EDWARD P. MURPHY,
United States District Judge

[Endorsed]: Filed July 23, 1956.

[Title of District Court and Cause.]

AMENDED COMPLAINT FOR WRONGFUL DEATH

Plaintiffs complain of defendant that:

I.

Prior to the filing of the complaint herein, plaintiff Ora Mae Birdsong was duly appointed the guardian ad litem of the plaintiffs Jerry Lee Birdsong and Dennis Birdsong;

II.

At all times mentioned herein relevant plaintiffs

were and are residents of the County of Alameda, State of California, within the jurisdiction of the above entitled court; this action is brought pursuant to the "Federal Tort Claims Act";

III.

At all times mentioned herein relevant defendant United States of America operated and controlled that certain Veterans Hospital located in the City of Oakland, County of Alameda, State of California;

IV.

Plaintiffs Ora Mae Birdsong, Jerry Lee Birdsong and Dennis Birdsong are the sole heirs at law of Thomas William Birdsong, deceased;

V.

On or about the 8th day of March, 1954, Thomas William Birdsong, deceased, was admitted to said Veterans Hospital for the treatment of ulcers and hypertension;

VI.

At said time and place the defendant, United States of America, had employed in said hospital certain physicians, surgeons, nurses and hospital aides; said physicians, surgeons, nurses and hospital aides were at all times herein mentioned acting within the course and scope of their employment;

VII.

On or about the aforesaid date, Thomas William Birdsong, deceased, was accepted as a patient by said physicians, surgeons, nurses and hospital aides,

and they and each of them undertook in their respective capacities to attend and cure the decedent;

VIII.

At said time and place, and thereafter until his death on April 11, 1954, said physicians and surgeons, nurses and hospital aides, who were then and there agents and employees of said defendant, United States of America, and who were acting within the course and scope of their employment, did not use proper care or skill in examining and endeavoring to cure and treat the decedent, in that no proper diagnosis was made prior to surgery to determine whether decedent was suffering from any condition that would contra-indicate surgery or anesthesia; and further, that pursuant to said undertaking, said defendant, United States of America, by and through its agents, treated said Thomas William Birdsong in a negligent and unskillful manner concerning that said operation performed on said decedent on March 10, 1954, in that said operation was performed under unsterile conditions and without proper pre-operative diagnosis as to the decedent's condition;

IX.

As a proximate result of defendant's negligent and unskillful examination and treatment of decedent as aforesaid, said Thomas William Birdsong languished and died on the 11th day of April, 1954;

X.

Decedent was an able bodied man, capable of,

and he did financially support his wife and children, the plaintiffs herein;

XI.

By reason of the premises, plaintiffs were compelled to and they did secure the services of duly licensed morticians and funeral homes, to their damage in a presently undetermined amount, which plaintiffs pray leave to insert by amendment when the same is determined;

XII.

By reason of the premises plaintiffs were deprived of the care, comfort, support, society, love and affection of Thomas William Birdsong, deceased;

XIII.

By reason of the premises, plaintiffs have been generally damaged in the sum of One Hundred Fifty Thousand Dollars ($150,000.00).

Wherefore, plaintiffs pray judgment against defendant as follows:

1. General damages in the sum of $150,000.00;
2. Special damages as may be alleged;
3. Costs of suit; and
4. Any further meet relief.

KAISER & O'NEILL,
/s/ By JEREMIAH F. O'NEILL, JR.,
Attorneys for Plaintiffs

Affidavit of Service by Mail attached.

[Endorsed]: Filed October 9, 1956.

[Title of District Court and Cause.]

NOTICE OF MOTION AND MOTION FOR MORE DEFINITE STATEMENT

To: Plaintiffs above named and their attorneys, Kaiser & O'Neill, Easton Building, Oakland 12, California.

You and each of you Will Please Take Notice that on Monday, December 3, 1956, at the hour of 9:30 a.m. or as soon thereafter as counsel may be heard, the defendant United States of America will, in the court room of the master calendar judge of the above-named court, Post Office Building, Seventh and Mission Streets, San Francisco, California, move for a more definite statement of the allegations contained in Paragraph VIII of plaintiffs' First Amended Complaint.

Said motion will be made pursuant to the provisions of Rule 12(b) of the Federal Rules of Civil Procedure, and will be based upon all the papers and records on file herein, and the defendant's memorandum of points and authorities filed herewith.

Dated: November 19, 1956.

LLOYD H. BURKE,
United States Attorney
/s/ By FREDERICK J. WOELFLEN,
Assistant United States Attorney

Notice of mailing attached.

[Endorsed]: Filed November 19, 1956.

[Title of District Court and Cause.]

ORDER FOR A MORE DEFINITE STATEMENT

The motion of the defendant United States of America for a more definite statement with respect to the allegations set forth in paragraph VIII of plaintiff's amended complaint came on regularly for hearing on December 3, 1956. The Court having been advised of the law and the premises, It Is Hereby Ordered that defendant's motion for a more definite statement be and the same is hereby granted.

Dated: December 4, 1956.

/s/ O. D. HAMLIN,
United States District Judge.

Notice of service by mail attached.

[Endorsed]: Filed December 4, 1956.

[Title of District Court and Cause.]

SECOND AMENDED COMPLAINT FOR WRONGFUL DEATH

Plaintiffs complain of defendant that:

I.

Prior to the filing of the complaint herein, plaintiff Ora Mae Birdsong was duly appointed the guardian ad litem of the plaintiffs Jerry Lee Birdsong and Dennis Birdsong;

II.

At all times mentioned herein relevant plaintiffs were and are residents of the County of Alameda, State of California, within the jurisdiction of the above entitled court; this action is brought pursuant to the "Federal Tort Claims Act";

III.

At all times mentioned herein relevant defendant United States of America operated and controlled that certain Veterans Hospital located in the City of Oakland, County of Alameda, State of California;

IV.

Plaintiffs Ora Mae Birdsong, Jerry Lee Birdsong and Dennis Birdsong are the sole heirs at law of Thomas William Birdsong, deceased;

V.

On or about the 8th day of March, 1954, Thomas William Birdsong, deceased, was admitted to said Veterans Hospital for the treatment of ulcers and hypertension;

VI.

At said time and place the defendant, United States of America, had employed in said hospital certain physicians, surgeons, nurses and hospital aides; said physicians, surgeons, nurses and hospital aides were at all times herein mentioned acting within the course and scope of their employment;

VII.

On or about the aforesaid date, Thomas William

Birdsong, deceased, was accepted as a patient by said physicians, surgeons, nurses and hospital aides, and they and each of them undertook in their respective capacities to attend and cure the decedent;

VIII.

At said time and place, and thereafter until his death on April 11, 1954, said physicians and surgeons, nurses and hospital aides, who were then and there agents and employees of said defendant, United States of America, and who were acting within the course and scope of their employment, did not use proper care or skill in examining and endeavoring to cure and treat the decedent, in that no proper diagnosis was made prior to surgery to determine whether decedent was suffering from any condition that would contra-indicate surgery or anesthesia; and further, that pursuant to said undertaking, said defendant, United States of America, by and through its agents, treated said Thomas William Birdsong in a negligent and unskillful manner concerning that said operation performed on said decedent on March 10, 1954, in that said operation was performed under unsterile conditions, in this, that the instruments used in said operation were unsterile, that the operating room and equipment therein were unsterile, and that no precautions were taken to prevent infection and disease from entering the operative wound;

IX.

As a proximate result of defendant's negligent

and unskillful examination and treatment of decedent as aforesaid, said Thomas William Birdsong languished and died on the 11th day of April, 1954;

X.

Decedent was an able bodied man, capable of, and he did financially support his wife and children, the plaintiffs herein;

XI.

By reason of the premises, plaintiffs were compelled to and they did secure the services of duly licensed morticians and funeral homes, to their damage in a presently undetermined amount, which plaintiffs pray leave to insert by amendment when the same is determined.

XII.

By reason of the premises plaintiffs were deprived of the care, comfort, support, society, love and affection of Thomas William Birdsong, deceased;

XIII.

By reason of the premises, plaintiffs have been generally damaged in the sum of One Hundred Fifty Thousand Dollars ($150,000.00).

Wherefore, plaintiffs pray judgment against defendant as follows:

1. General damages in the sum of $150,000.00;
2. Special damages as may be alleged;
3. Costs of suit; and

4. Any further meet relief.

KAISER & O'NEILL,

/s/ By JEREMIAH F. O'NEILL, JR.,
Attorneys for Plaintiffs

Affidavit of Service by Mail Attached.

[Endorsed]: Filed April 18, 1957.

[Title of District Court and Cause.]

ANSWER TO SECOND AMENDED COMPLAINT

Comes now defendant United States of America and answers the Second Amended Complaint of plaintiffs as follows:

Answering paragraphs V, VI, VII, VIII, IX, X, XI and XII, this answering defendant denies, generally and specifically, each and every, all and singular, the allegations therein contained and the whole thereof, and further denies that plaintiffs were damaged in the sum of $150,000, or in any other sum or amount whatsoever.

Wherefore, defendant prays that plaintiffs take nothing by their said complaint, and that said complaint be dismissed with defendant's cost of suit herein incurred and such other and further relief as to the Court may be meet and proper in the premises.

Dated: May 6, 1957.

LLOYD H. BURKE,
United States Attorney
/s/ FREDERICK J. WOELFLEN,
Assistant United States Attorney
Attorneys for Defendant

Affidavit of Service by Mail attached.

[Endorsed]: Filed May 7, 1957.

[Title of District Court and Cause.]

INTERROGATORIES PROPOUNDED BY UNITED STATES OF AMERICA, TO BE ANSWERED UNDER OATH, IN TRIPLICATE, WITHIN 15 DAYS OF RECEIPT BY PLAINTIFF ORA MAE BIRDSONG

If any of the following interrogatories cannot be answered in full, please answer to the extent possible, specifying the reason for your inability to answer the remainder, and stating whatever information or knowledge you have concerning the unanswered portion. It is requested that the United States Attorney be supplied with three copies of your answers.

1. Please identify yourself by giving full name, age, residence and occupation.

2. Please state the full name, age, occupation and last residence of the deceased.

3. Please give all addresses at which deceased

resided for the five years immediately preceding death.

4. Please state your relationship, if any, to decedent.

5. Please give names, ages and addresses of all of the heirs, and next-of-kin of decedent, and the relationship of each individual to the decedent.

6. Did the decedent leave a will?

7. If your answer to the preceding interrogatory is in the affirmative, please state when, where and in what court said will was presented for probate.

8. If the decedent had any accidents, illnesses or disease within ten years prior to the date of the accident alleged in your declaration, please state fully:

(a) The nature of such accidents, illnesses or diseases;

(b) When and where they were sustained or suffered;

9. Please give the names and addresses of any person or persons to whom deceased resorted, or consulted by deceased, to obtain medical care, advice or attention within the ten years immediately preceding death.

10. Please give the name and address of each hospital, sanitorium, clinic, health farm or rest home, in which the decedent received medical care, advice or treatment within the ten years immediately preceding death.

11. Please state the name and address of the employer of the decedent prior to the happening of the accident.

12. If the decedent was self-employed, please state the name and address of the firm or business under which the business or profession was operated.

13. If the decedent was self-employed, please indicate whether such employment was as an individual or in partnership, or other association, with others.

14. If your answer to the preceding interrogatory is to the effect that the decedent was engaged in a partnership, or other association, with others, please give:

(a) The names and addresses of all partners or associates of the decedent;

(b) The type of business or occupation engaged in by said partnership or other association, its firm name and style, and the address of its principal place of business.

15. If the decedent, immediately prior to or at the time of death, was employed by a corporation, or for a salary, or for wages, please state:

(a) The average amount of the decedent's weekly or monthly salary or wages, on the basis of the last five (5) years' employment;

(b) The name and address of the employer of the decedent;

(c) The names and addresses of all employers of the decedent in the five (5) years prior to death;

(d) The exact weekly, monthly, or annual wage received by decedent at the time of death;

(e) The exact weekly, monthly, or annual wage

received from each employer of the decedent in the five (5) years prior to death.

16. If the deceased was self-employed, please state:

(a) The average income from the business or profession of the decedent, on the basis of the five (5) years prior to death;

(b) The income from the business or profession of the decedent:

(1) In the calendar year 1951;

(2) In the calendar year 1952;

(3) In the calendar year 1953.

17. If the deceased was engaged in a partnership, or other association, with others, please state:

(a) The average income from the partnership, or other association, on the basis of the five (5) years prior to death.

(b) The income from the partnership or other association:

(1) In the calendar year 1951;

(2) In the calendar year 1952;

(3) In the calendar year 1953.

18. Did the decedent obtain or receive income from any source other than from business, profession, occupation, wages or salary in the five (5) years prior to death?

19. If your answer to the preceding interrogatory is in the affirmative, please itemize such income:

(a) Received in the calendar year 1950;

(b) Received in the calendar year 1951;

(c) Received in the calendar year 1952;

(d) Received in the calendar year 1953.

20. Did the deceased leave next-of-kin who were dependent upon him for support:

(a) Wholly?

(b) In part?

21. If your answer to the preceding interrogatory is in the affirmative, please give the names, ages and addresses of all such persons and the relationship of each to the deceased.

22. If your answers to interrogatory number 20 is in the affirmative, please itemize the amount paid or contributed to the aid or support of any dependent:

(a) In the calendar year 1951;

(b) In the calendar year 1952;

(c) In the calendar year 1953.

23. Please state the value of the decedent's estate at the date of death.

24. Prior to the admission of Thomas Birdsong to the Veterans Administration Hospital on March 8, 1954, had he been hospitalized within the preceding five years for any difficulty or complaints pertaining to his stomach, heart, kidneys, bladder, or for a nervous disorder? If so, state:

(a) The hospitals to which he was admitted, with dates of admission and discharge;

(b) The names and addresses of attending physicians;

(c) The specific medical complaints for which he was treated.

25. Within the five years immediately preceding March 8, 1954, had Thomas Birdsong been under the care of any physician or surgeon with respect to stomach, heart, kidneys, bladder, or for nervous disorders or complaints which did not require his being hospitalized? If so, state:

(a) The names and addresses of the physicians who attended him;

(b) The specific medical complaints for which he was treated.

26. At any time within the five years immediately preceding March 8, 1954, had Thomas Birdsong been confined to a hospital as a result of any cardiac or cardiovascular difficulty? If so, state:

(a) The hospitals to which he was so confined, with dates of admission and discharge;

(b) The names and addresses of attending physicians;

(c) The specific medical complaints for which he was hospitalized.

27. At any time within the five years immediately preceding March 8, 1954, had Thomas Birdsong been under the care of a physician for cardiac or cardiovascular complaints which did not require confinement in a hospital? If so, state:

(a) The names and addresses of the doctors who so attended him;

(b) The approximate periods of time he was under the care of such doctors;

(c) The specific medical complaint for which he was treated.

28. At any time between March 8, 1954 and April 11, 1954, while Thomas Birdsong was confined to the Veterans Administration Hospital in Oakland, California, was he examined by any private physician who was not an employee of the Veterans Administration or who was not a consultant for said hospital? If so, state:

(a) The name of the doctor who so examined him;

(b) Said doctor's relationship to Thomas Birdsong and to you;

(c) When such examination took place;

(d) Whether you or your attorney has in your possession or control any medical report by said doctor covering said examination. If so, will you kindly attach a copy of the report to your answers, thus obviating the necessity for defendant's moving the Court for production of same.

29. At any time while Thomas Birdsong was confined in the Veterans Administration Hospital in Oakland between March 8, 1954 and April 11, 1954, was any private physician (not an employee of the Veterans Administration and not acting as consultant thereto) called into consultation with any of the physicians who were then attending Thomas Birdsong for any of the conditions for which he was confined to said hospital? If so, kindly state such doctor's name, his address, and his relationship to either you or Thomas Birdsong, if any.

30. If such consultation occurred, kindly state:

(a) The medical condition of Thomas Birdsong for which he was called into consultation;

(b) Whether the physician who was called into consultation prepared a report setting forth his diagnosis and prognosis of Thomas Birdsong's condition;

(c) Whether, if either you or your attorney has within your custody or control such consultation report, you will voluntarily attach a copy of it to the answers hereto (thus eliminating the necessity for defendant's moving the Court for its production).

31. Were you at any time orally advised by any doctor who examined Thomas Birdsong while he was confined at the Oakland Veterans Administration Hospital from March 8, 1954, to April 11, 1954, concerning his condition and the prognosis for his recovery? If so, please state:

(a) When you were so advised;

(b) The name and address of the doctor who discussed this matter with you;

(c) Such doctor's relationship to you or Thomas Birdsong;

(d) Where such discussion took place;

(e) What, in substance, you were orally advised by said doctor.

32. Were you ever orally advised by any physician who attended, treated and cared for Thomas Birdsong in the Oakland Veterans Administration Hospital between March 8, 1954, and April 11, 1954, as to the result of said physician's examination, treatment and operative procedure, and as to his diagnosis and prognosis regarding your husband's

condition and his chances for recovery? If so, please state:

(a) When you were so advised;

(b) The name and address of the physician who so advised you;

(c) His relationship, if any, to either you or Thomas Birdsong:

(d) The substance of what you were so advised.

33. Are you or any of the decedent's heirs or next-of-kin receiving any death benefits from any agency of the U. S. Government, State of California, or municipality arising out of the death of Thomas Birdsong which occurred on April 11, 1954? If so, state:

(a) From whom you are receiving the benefits;

(b) The amount each person is receiving either per week, per month, or per year by way of benefits;

(c) When the payments in question commenced.

34. Following the death of Thomas Birdsong on April 11, 1954, did you discuss with any doctor, nurse, medical aid or attendant, or employee of the Veterans Administration Hospital, Oakland, California, or with the Veterans Administration Regional Office, San Francisco, California, the nature, extent and results of any and all medical treatment, diagnostic tests, clinical studies, pathology procedures and reports, operative and surgical procedures, consultations, diagnosis and prognosis given, made, administered or undertaken, concerning Thomas Birdsong's physical condition and

illness which occurred during his confinement in the Veterans Administration Hospital, Oakland, California, from March 8, 1954 to April 11, 1954? If so, state:

(a) The names and addresses, and relationship to you of the person or persons with whom you had such discussions.

(b) When and where these discussions took place.

(c) What you were told.

35. At any time following the death of Thomas Birdsong on April 11, 1954, did any doctor of your own choosing, or as a volunteer in your behalf, review and inspect the medical records and files of the Veterans Administration Hospital, Oakland, California, covering your late husband's confinement in that institution from March 8, 1954, to April 11, 1954?

36. If your answer to the foregoing interrogatory is in the affirmative, kindly state:

(a) The name and address of the doctor who inspected or reviewed these medical records and files.

(b) When and where the doctor reviewed and inspected these records and files.

(c) If you received a verbal or written report from said doctor concerning his medical findings and opinions regarding the medical treatment your husband received and your husband's physical condition, and his chances for recovery, based upon said doctor's examination and recommendations in the Veterans Administration Hospital's records and files.

(d) If said report was written, kindly attach a copy thereof to your answer to these interrogatories.

37. Subsequent to your husband's death in the Oakland Veterans Administration Hospital on April 11, 1954, have you discussed or received any information from any doctor, private consultant, medical aid or attendant, or employee of the Veterans Administration concerning the existence of unsanitary conditions, the use of unsanitary instruments and equipment, and the lack of proper precautions being used to prevent infection and disease during your husband's operation of March 10, 1954 at the Veterans Administration Hospital, Oakland, California? If so, state:

(a) The names and addresses and relationship to you of all persons with whom you discussed this matter or who supplied you with information regarding the conditions mentioned above.

(b) If you or your attorneys have any written reports regarding the subject of this interrogatory, list the names and addresses of the person or persons who supplied or furnished such a report.

38. If your answer to the foregoing interrogatory is in the negative, kindly state the source of information which is the basis of your allegation in Paragraph VIII of Second Amended Complaint which reads as follows:

"That pursuant to said undertaking, said defendant United States of America, by and through its agents, treated said Thomas William Birdsong in a negligent and unskillful manner concerning that

said operation performed on said decedent on March 10, 1954 in that said operation was performed under unsterile conditions, in this, that the instruments used in said operation were unsterile, that the operating room and equipment therein were unsterile, and that no precautions were taken to prevent infection and disease from entering the operative wound."

39. Subsequent to your husband's death in the Veterans Administration Hospital, Oakland, on April 11, 1954, have you discussed with, or received any information from, any doctor, private consultant, nurse, medical aid or attendant, or employee of the Veterans Administration indicating that the physicians, surgeons, nurses and hospital aids at the Veterans Administration Hospital, Oakland, California, did not use proper care or skill in examining and endeavoring to cure and treat your husband—particularly, that they did not make a proper diagnosis prior to surgery performed upon him to determine whether your husband was suffering from any condition that would contra-indicate surgery or anaesthesia? If so, state:

(1) The names and addresses and relationship to you of all persons with whom you have discussed this matter, or who supplied you with information regarding the conditions mentioned above.

(2) If you have any written reports regarding the subject matter of this interrogatory, list the names and addresses of the person or persons who supplied you with such a report.

40. If your answer to the foregoing interrogatory

is in the negative, kindly state the source of the information which is the basis of your allegation as contained in Paragraph VIII of the Second Amended Complaint which states:

"At said time and place, and thereafter until his death on April 11, 1954, said physicians and surgeons, nurses and hospital aids, were then and there agents and employees of said defendant United States of America, and who were acting within the course and scope of their employment, did not use proper care or skill in examining and endeavoring to cure and treat the decedent, in that no proper diagnosis was made prior to surgery to determine whether decedent was suffering from any condition that would contra-indicate surgery or anaesthesia;"

41. With respect to the allegations contained in paragraph VIII of your Second Amended Complaint, state with particularity:

(a) The names and identities of all physicians and surgeons, nurses and hospital aids who were employees of the U. S. Government at the Veterans Administration Hospital, Oakland, California, from March 8, 1954 to April 11, 1954, who did not use proper skill in examining and endeavoring to cure and treat your husband, who did not make a proper diagnosis prior to your husband's surgery, to determine whether he was suffering from any condition that would contra-indicate surgery or administration of an anaesthesia, or who used unsterile, operative equipment, who allowed the operating room and its equipment to be used in an

unsterile condition, and who took no precautions to prevent infection and disease from entering your husband's operative wound.

(b) The exact nature of said negligence and carelessness, and name all the acts or omissions committed by each of said surgeons, physicians, nurses and hospital aids in each of the alleged negligent circumstances mentioned in paragraph VIII.

Dated: May 16, 1957.

LLOYD H. BURKE,
United States Attorney
/s/ By FREDERICK J. WOELFLEN,
Assistant United States Attorney

Affidavit of Service by Mail attached.

[Endorsed]: Filed May 17, 1957.

United States District Court for the Northern District of California, Southern Division

No. 35390—Civil

JERRY LEE BIRDSONG and DENNIS BIRDSONG, by and through their guardian ad litem, ORA MAE BIRDSONG, and ORA MAE BIRDSONG, Plaintiffs,

vs.

UNITED STATES OF AMERICA, Defendant.

ORDER OF DISMISSAL

At a Stated Term of the United States District Court for the Northern District of California,

Southern Division, held at the Court Room thereof, in the City and County of San Francisco, on Wednesday, the 23rd day of April, in the year of our Lord one thousand nine hundred and fifty-eight.

Present: the Honorable Louis E. Goodman.

This case came on regularly this day for dismissal for lack of prosecution.

Ordered said case dismissed for lack of prosecution.

[Title of District Court and Cause.]

NOTICE OF MOTION AND MOTION TO SET ASIDE DISMISSAL FOR LACK OF PROSECUTION

To the Defendant, United States of America, and to Lloyd H. Burke and Frederick J. Woelflen, attorneys for defendant:

You and Each of You Please Take Notice that on Monday, the 9th day of June, 1958, at 9:30 o'clock a.m., in the Law and Motion Department, Court House, Seventh and Mission, San Francisco, California, plaintiffs will move the above entitled court for an order setting aside and vacating the order of dismissal heretofore entered on April 23, 1958, on the grounds that said order was made through the inadvertence and excusable neglect on the part of plaintiffs' attorneys, and further on the grounds that the interests of justice would be served thereby.

Said motion will be based on this Notice of

Motion, upon the affidavit of Jeremiah F. O'Neill, Jr. attached hereto and made a part hereof, and upon all the records and papers on file herein.

Dated: May 28, 1958.

KAISER & O'NEILL,
/s/ By JEREMIAH F. O'NEILL, JR.,
Attorneys for Plaintiffs

Affidavit of Service by Mail attached.

[Endorsed]: Filed June 2, 1958.

[Title of District Court and Cause.]

AFFIDAVIT OF JEREMIAH F. O'NEILL, JR.

State of California,
County of Alameda—ss.

Jeremiah F. O'Neill, Jr., being duly sworn, deposes and says: That he is an attorney licensed to practice before the above entitled court, and is one of the attorneys for the plaintiffs herein;

That plaintiffs employed your affiant's office to prosecute the within action shortly before April 10, 1956, and that your affiant caused the original Complaint herein to be filed on the 10th day of April, 1956;

That defendant's answer to the second amended complaint was filed in May of 1957, and that thereafter defendant served 41 written interrogatories upon plaintiffs; that plaintiff Ora Mae Birdsong is a widow with two small sons, and at the time the

interrogatories were served upon this office was employed six days a week, and subsequently found it very difficult to present herself in affiant's office for the purpose of answering interrogatories; that because of this difficulty, the interrogatories were answered on August 29, 1957;

That on December 17, 1957, your affiant wrote a letter to Mr. Frederick J. Woelflen, one of the attorneys for the defendant herein, requesting that depositions of the Custodian of Records of the Veterans Administration Hospital and the doctors involved be taken, a copy of which letter is attached hereto and incorporated herein by reference; that in said letter your affiant requested that he be advised whether the depositions could be taken by stipulation, or whether the United States Attorney's Office requests notice of depositions to be taken; that within a few days after sending the letter above referred to, your affiant received a telephone call from Mr. Woelflen to discuss the subject matter of the letter; that at said time Mr. Woelflen stated to your affiant that the defendant was willing to have the depositions taken by stipulation, but that the whereabouts of some of the doctors might not be known since the possibility existed that some of them were no longer with the Veterans Administration Hospital; Mr. Woelflen further stated that because of this problem, it would probably take considerable time for him to locate the doctors and arrange for the taking of their depositions, and that he would contact your affiant when the same were arranged;

That, relying upon the statements of Mr. Woelflen, your affiant inadvertently filed the case away, and due to the press of business, did not do anything further with reference to the taking of the depositions while waiting to hear further from Mr. Woelflen; that because of Mr. Woelflen's statement that considerable time would be necessary to contact the doctors, your affiant was not worried about the passage of time until the notification that the case would appear on the dismissal calendar; that at that time your affiant again telephoned Mr. Woelflen and was advised by him for the first time that the doctors were not available; that had your affiant known that the doctors were not available, he would have proceeded with the deposition of the Custodian of Records of the Veterans Administration Hospital, as well as taking investigative steps to locate the doctors;

That your affiant feels that the length of time during which no steps were taken in the within case were due to inadvertence and excusable neglect on his part. Your affiant feels that the plaintiffs have a valid cause of action and that the best interests of justice will be served by setting aside the order of dismissal and allowing the matter to be heard on its merits.

/s/ JEREMIAH F. O'NEILL, JR.

Subscribed and sworn to before me this 29th day of May, 1958.

[Seal] /s/ LUCILLE T. HALL,

Notary Public in and for County of Alameda, State of California.

Mr. Frederick J. Woelflen Dec. 17, 1957
Assistant U. S. Attorney
422 Post Office Building, Seventh and Mission
San Francisco 1, California

Re: Birdsong vs. U. S., Civil No. 35390.

Dear Mr. Woelflen:

I would like very much to take the depositions of the doctors involved in the above case, as well as the Custodian of Records of the VA Hospital in Oakland.

The doctors' names that I presently have are a Dr. Moore and a Dr. Schoenberger, and I think that perhaps the best way to proceed would be to take the deposition of the Custodian of Records first, so that we may thereby ascertain the names of any other doctors involved.

Would you kindly advise whether these matters can be disposed of by stipulation or whether it is necessary for your office to have noticed depositions set up.

Thank you for your cooperation. Best wishes.

Very truly yours,

KAISER & O'NEILL,
By .....,
JFO:lh Jeremiah F. O'Neill, Jr.

[Endorsed]: Filed June 2, 1958.

[Title of District Court and Cause.]

NOTICE OF APPEAL

To: The Honorable Louis E. Goodman, Judge of the United States District Court for the Northern District of California, Southern Division.

Plaintiffs Jerry Lee Birdsong and Dennis Birdsong, by and through their guardian ad litem, Ora Mae Birdsong, and Ora Mae Birdsong, hereby appeal from that order of the above entitled Court and the Honorable Louis E. Goodman, Judge thereof, made and entered in the above entitled matter on the 23rd day of April, 1958, dismissing the within action, and further appeal from that order denying plaintiffs' motion to set aside dismissal for lack of prosecution made and entered on June 11, 1958.

This notice is filed for the purpose of complying with the requirements of the provisions of Rule 73 (b), Rules on Appeal.

Dated: June 12, 1958.

KAISER & O'NEILL,
/s/ By JEREMIAH F. O'NEILL, JR.,
Attorneys for Plaintiffs

Affidavit of Service by Mail attached.

[Endorsed]: Filed June 13, 1958.

[Title of District Court and Cause.]

UNDERTAKING FOR COSTS ON APPEAL

Whereas, the above entitled Plaintiffs, Jerry Lee Birdsong, and Dennis Birdsong, by and through their guardian ad litem Ora Mae Birdsong, and Ora Mae Birdsong, are about to appeal to the United States Circuit Court of Appeals for the Ninth Circuit, from a judgment entered against them in said action in said District Court of the United States, Northern District of California, Southern Division on April 23, 1958 and June 11, 1958.

Now, Therefore, in consideration of the premises and of such appeal, the undersigned, Standard Accident Insurance Company, a corporation, organized and existing under and by virtue of the laws of the State of Michigan, and duly authorized and licensed to transact a general surety business in the State of California, does hereby undertake and promise on the part of the Appellants, that said Appellants will pay all costs which may be awarded against them on the appeal, or on a dismissal thereof, not exceeding the sum of Two Hundred Fifty and 00/100 ($250.00) Dollars, to which amount it acknowledges itself bound.

It Is Further Stipulated as a part of the foregoing bond, that in case of the breach of any condition thereof, the above named District Court may upon ten (10) days notice to the surety, Standard Accident Insurance Company, above named, pro-

ceed summarily in said action or suit, to ascertain the amount which said surety is bound to pay on account of such breach, and render judgment therefor against said surety and award execution therefor.

Signed and Sealed at Oakland, California, this 12th day of June, 1958.

[Seal] STANDARD ACCIDENT INSURANCE COMPANY,

/s/ By J. P. SIMPSON,
Attorney in fact

Premium charged $10 per annum

Affidavit of Verification attached.

[Endorsed]: Filed June 13, 1958.

[Title of District Court and Cause.]

ANSWER TO INTERROGATORIES

1. Ora Mae Birdsong, age 30. 1228 - 103rd Ave., Oakland, Calif. Cashier, Schaffner & Watson, San Leandro, Calif.

2. Thomas Birdsong, age 30. Transformer Assembly, Electro Engineering, San Leandro, Calif. 10429 Royal Ann, Oakland, Calif.

3. 10429 Royal Ann, Oakland, Calif. 1228 - 103rd Ave., Oakland, Calif.

4. Widow.

5. Jerry Lee Birdsong, son, age 11, 1228 - 103rd Ave., Oakland, Calif. Dennis Birdsong, son, age 10, 1228 - 103rd Ave., Oakland , Calif. Grace Birdsong,

mother, Decatur, Alabama. Newt Birdsong, father, Decatur, Alabama. Charles Birdsong, brother, Decatur, Alabama. Judy Smith, sister, Decatur, Alabama. Opal Terry, sister, Decatur, Alabama. Ann Wasiewicz, sister. Charlotte Robbins, sister, Decatur, Alabama.

6. No.

7. .....

8. No accidents. Illnesses—high blood pressure, ulcers—service connected. Other illnesses unknown.

9. Dr. Paul Rahn, 515 Estudillo, San Leandro, Calif. Veterans Hospital, Oakland, Calif. A psychiatrist, name forgotten, to whom deceased was referred by Veterans Administration.

10. Veterans Hospital, Oakland, Calif.

11. Electro Engineering, 401 Preda, San Leandro, Calif.

12. Not self employed.

13. Not self employed.

14. Not self employed.

15. (a) Approximately $4000.00 yearly. (b) Electro Engineering, 401 Preda, San Leandro, Calif. (c) General Electric Co., 5441 E. 14th St., Oakland, Calif., Electro Engineering, 401 Preda, San Leandro, Calif. (d) Unknown. (e) Unknown.

16. Not self employed.

17. Not self employed.

18. No.

19. .....

20. None other than widow and two sons, who are plaintiffs.

21. .....

22. .....

23. No estate.

24. (a) Veterans Hospital, Oakland, Sept. 1948, August, 1949, and periodically until March 8, 1954. (b) Unknown—various physicians at Veterans Hospital, Oakland. (c) Hypertension and ulcers.

25. (a) Dr. Paul Rahn, 515 Estudillo, San Leandro, Calif. (b) Hypertension and ulcers.

26. All hospitalizations have been at the Veterans Hospital, Oakland, Calif., as stated in Answer 24.

27. The only other physician involved was Dr. Paul Rahn, 515 Estudillo, San Leandro, Calif., as stated in Answer 25.

28. No.

29. Not to my knowledge.

30. .....

31. (a) During hospitalization, March 8-April 11, 1954. (b) Unknown. (c) Doctors at Veterans Hospital, Oakland, Calif. (d) At Veterans Hospital, Oakland, Calif. (e) I was advised that my husband had ulcers, necessitating surgery; that his blood pressure was high and as soon as it leveled off he would be taken to surgery. Before surgery, I was told not to get my hopes up; after surgery I was advised that he was doing well. On April 11, 1954, I was told that my husband didn't have long, and I was advised to call his family.

32. See Answer 31.

33. (a) Veterans Administration. (b) $150.00 a month for myself and two sons. (c) Approximately November, 1955.

34. (a) 1. Dr. Moore, Veterans Hospital, Oakland, Calif.; 2. Veterans Administration, San Francisco, Calif. (b) 1. At Veterans Hospital, Oakland, within two or three months after April 11, 1954; 2. On telephone within four months after April 11, 1954. (c) 1. That in his opinion my husband's illness had gone back for a long time and that I should have the American Legion representative at hospital contact him; 2. Advised first how to obtain autopsy report and after I advised them I was unable to obtain it through regular channels, that the report would be of no value to me any way, because I wouldn't understand it if I had it.

35. No.

36. .....

37. No.

38. At the time of my husband's confinement at the hospital, I personally observed filth and dirt everywhere; there was dirt and fuzz under the beds; filled urinals were allowed to remain under the beds all day, and the entire operation of the hospital was filthy and unsterile.

39. No.

40. I was advised by my attorney that if my husband had hepatitis before surgery, that my doctor should know that his liver could not tolerate anesthesia.

41. (a) The doctors who performed the surgery were Dr. Moore and Schoenberger of the Veterans Hospital, Oakland. The names of the other doctors, nurses, hospital aids and other employees are not known to me, but are probably contained in the

medical records at the hospital. (b) 1. If my husband had hepatitis prior to surgery, proper medical procedures would have diagnosed the condition; 2. If the doctors knew that my husband had hepatitis prior to surgery, proper medical procedure would have indicated that the liver could not tolerate anesthesia.

KAISER & O'NEILL,
/s/ By JEREMIAH F. O'NEILL, JR.,
Attorneys for Plaintiffs

Affidavit of Service by Mail attached.

[Endorsed]: Filed June 13, 1958.

[Title of District Court and Cause.]

APPELLANTS' STATEMENT OF POINTS AND DESIGNATION OF RECORD

To: The Honorable United States District Court for the Northern District of California, Southern Division:

Plaintiffs Jerry Lee Birdsong and Dennis Birdsong, by and through their guardian ad litem, Ora Mae Birdsong, and Ora Mae Birdsong, in accordance with Rule 75 (a) of the Rules of Civil Procedure, hereby file Appellants' Statement of Points and Designation of Record in the above entitled cause as follows:

That the Honorable Court erred in dismissing the within action for lack of prosecution on April 23, 1958.

Appellants hereby designate the following portions of the record to be contained in the Record on Appeal:

The Complaint, the First Amended Complaint, the Second Amended Complaint, the Answer to the Second Amended Complaint, the Affidavit of Service by Mail of the Answers to Interrogatories, the Notice of Motion and Motion to Set Aside Dismissal for Lack of Prosecution, the Affidavit of Jeremiah F. O'Neill, Jr. in Support of said Motion, together with the copy of the letter attached to said Affidavit and incorporated therein by reference.

Appellants hereby designate the following portion of the reporter's record to be contained in the Record on Appeal:

All oral proceedings had on the proceedings for dismissal for lack of prosecution on April 23, 1958, and all oral proceedings had on the motion to set aside dismissal for lack of prosecution on June 11, 1958.

Dated: June 12, 1958.

KAISER & O'NEILL,
/s/ By JEREMIAH F. O'NEILL, JR.,
Attorneys for Plaintiffs

[Endorsed]: Filed June 13, 1958.

[Title of District Court and Cause.]

COUNTER-DESIGNATION OF RECORD ON APPEAL

The defendant United States of America does herewith counter-designate the record on appeal in the above matter as follows:

All papers, pleadings, motions, orders and notices on file with the Clerk of the United States District Court in said matter, together with the Clerk's Docket Sheet showing all entries made during the pendency of this proceeding.

Dated: June 13, 1958.

LLOYD H. BURKE,
United States Attorney
/s/ FREDERICK J. WOELFLEN,
Assistant U. S. Attorney

Affidavit of Service by Mail attached.

[Endorsed]: Filed June 13, 1958.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, C. W. Calbreath, Clerk of the United States District Court for the Northern District of California, hereby certify the foregoing and accompanying documents and exhibits, listed below, are the originals filed in this Court in the above-entitled case and constitute the record on appeal herein as

designated by counsel for the Appellants and the Appellee:

Excerpt from Docket Entries.

Complaint.

Petition for and Order Appointing Guardian Ad Litem.

Motion of Defendant for More Definite Statement.

Order Granting Motion for More Definite Statement.

Amended Complaint for Wrongful Death.

Notice by Defendant for More Definite Statement.

Order for More Definite Statement.

Second Amended Complaint.

Answer of Defendant to Second Amended Complaint.

Interrogatories by Defendant to Ora Mae Birdsong.

Order Dismissing case for Lack of Prosecution.

Notice and Motion by Plaintiffs to Set Aside Dismissal.

Affidavit of Jeremiah F. O'Neill, Jr. in Support of Motion to Set Aside Dismissal.

Notice of Appeal.

Appeal Bond.

Statement of Points Upon Which Appellants Intend to Rely on Appeal.

Answer of Plaintiff Ora Mae Birdsong to Interrogatories by Defendant.

Counter-designation of Appellee of record on appeal.

In Witness Whereof I have hereunto set my hand and affixed the seal of said District Court this 18th day of July, 1958.

[Seal] C. W. CALBREATH,
Clerk
/s/ By MARGARET P. BLAIR,
Deputy Clerk

[Title of District Court and Cause.]

PROCEEDINGS FOR DISMISSAL FOR LACK OF PROSECUTION

April 23, 1958

Before: Hon. Louis E. Goodman, Judge.

Appearances: For the Plaintiff: Messrs. Kaiser & O'Neill, by Jeremiah F. O'Neill, Jr. For the Defendant: Hon. Lloyd H. Burke, U. S. Attorney, by Frederick J. Woelflen, Esq., Assistant U. S. Attorney.

The Clerk: Birdsong, et al., versus the United States.

Mr. O'Neill: Jeremiah O'Neill for the plaintiff.

Mr. Woelflen: Frederick Woelflen for the defendant, the United States.

Mr. O'Neill: If Your Honor please, in this matter on December 17, of '57, I wrote to Mr. Woelflen to see if we could arrange by stipulation the taking of certain depositions of doctors involved in this matter, as well as the hospital records of the Oakland Veterans Hospital.

At that time, he returned our call, to me, telling me that he would attempt to find the doctor. This matter occurred back in 1954; that he would attempt to locate this doctor.

The Court: Is this another mal-practice case?

Mr. O'Neill: It is a wrongful death case, Your Honor.

Mr. Woelflen: I might call Your Honor's attention to the facts. The incident which is the basis of this suit, occurred on April 11, 1954. The suit was filed on April 10, 1956, one day short of the running of the Statute of Limitations.

On June 12, 1956, we filed a motion for a more definite statement, which Judge Murphy granted on July 23, 1956.

The first amended complaint in this action was not trialed until October 8, 1956, approximately two and a half months later.

On November 19, 1956, we filed a motion for a more definite statement on the second amended complaint. Judge Hamlin granted that motion on December 4, 1956.

The second amended complaint was not filed until April 17, 1957, a year after the original complaint was filed, three years after the alleged mal-practice.

We have thereafter, on May 7th, filed interrogatories which were required to be answered in 15 days, and they were not filed until August 29, 1957.

Now, it is true counsel asked me something about doctors in December of 1957, and at that time I advised him that several of our doctors were not available; and in checking the record this morning,

I find that other doctors are no longer in the service of the Government.

I think that this case—I realize counsel's position, but I think that this case is one that is ripe for dismissal, in view of the fact that the incidents which are the basis of this complaint, occurred over four years ago.

Mr. O'Neill: I state, Your Honor, that this is a matter that did not come into my office until just shortly before the case was filed. The case was filed immediately upon receipt in my office.

It involves the death of a young father, and there are two minor children involved.

I have realized the position we are in as far as the doctors are concerned. We have attempted everything in our power to find out where these doctors are, and I just heard this morning from Mr. Woelflen that he now doesn't know where these doctors are.

I was under the impression when I talked to him on the phone that he would attempt to make them available.

If Your Honor would allow me to file a memo under these circumstances, especially involving minors, I will proceed to trial.

The Court: But apparently you don't even know whether you have got a case.

Mr. O'Neill: We will go to trial, Your Honor, on the hospital records, together with the witnesses I intend to call.

The Court: Well, I think this case is just too old.

Mr. O'Neill: Your Honor, it has not appeared

on any calendar prior to this; and if the doctors are unavailable for us, I am willing to go to trial on the hospital records, together with the witnesses I have.

The Court: What witnesses have you got?

Mr. O'Neill: I expect to call a medical witness, Your Honor, a medical expert witness on this matter.

The Court: How can a medical expert witness testify to something when there aren't going to be witnesses to testify for the Government?

Mr. O'Neill: On the hospital records, and on the operative reports, Your Honor.

The Court: How could a judge pass on anything like that? How could anyone give credence to any expert testimony of a man who was going to testify on some writings that somebody put on a piece of paper four years ago?

Mr. O'Neill: These are writings that would be put there, Your Honor, by the doctors who performed the work.

The Court: Obviously you weren't able to plead your cause, because you had to file two amended complaints to show the alleged mal-practice. This case is too old. I will grant the motion to dismiss.

[Endorsed]: Filed August 14, 1958.

[Title of District Court and Cause.]

PROCEEDINGS ON MOTION TO SET ASIDE DISMISSAL FOR LACK OF PROSECUTION

June 11, 1958

Before: Hon. Louis E. Goodman, Judge.

Appearances: For the Plaintiff: Jeremiah F. O'Neill, Jr. For the Defendant: Frederick J. Woelflen, Esq., Assistant U. S. Attorney.

The Clerk: Birdsong, versus United States, motion to vacate dismissal. Counsel state their appearances for the record.

Mr. O'Neill: Jeremiah O'Neill, Your Honor, for the plaintiffs.

Mr. Woelflen: Frederick J. Woelflen, for the United States.

Mr. O'Neill: May I proceed, Your Honor?

The Court: Yes.

Mr. O'Neill: Thank you. If Your Honor please, this matter came up on the last dismissal calendar. It was the first time it had appeared on the dismissal calendar, and Your Honor made an order that the matter be dismissed.

I am appearing here today on a motion to vacate that order, Your Honor, on the basis that any delay that was taken in this particular matter was not intentional, and was not due to—was because of inadvertence on my part.

If Your Honor please, I had arranged back in December of last year, with Mr. Woelflen, for the

taking of depositions of the custodian of records of the Veterans Hospital in Oakland, as well as certain doctors that were involved in this matter.

This is not a case, Your Honor, of mal-practice on the physician himself, but rather, a case involving the conditions at the hospital. So that there is no problem about any particular act of any particular doctor involved.

However, Mr. Woelflen advised me at that time that he would attempt to locate the doctors, but that it may be some period of time before he could, and that he would be glad to proceed by stipulation with the deposition of the custodian of records, and also of the hospital.

I don't mean in any way to infer, Your Honor, that Mr. Woelflen misled me in any way. He was most courteous and most gracious throughout our dealings, all through this case. But because of that, his indication that there would be considerable delay in finding the doctors, I did nothing further until I heard from him, as to when the doctors would be available.

Had it not been for that, Your Honor, I would have proceeded to take the deposition of the custodian of records, and proceeded to have the matter placed on the trial calendar for trial.

I feel that—It's a case where we have a young widow, Your Honor, of about 32 years of age, with two small boys. I feel that the interest of justice would be served in allowing the case to be heard on its merits, and I feel that I could, within 30 days, have the matter completely ready for trial,

Your Honor, and I earnestly move the Court that I be given permission to have the case heard on its merits.

The Court: Well, counsel, this was argued at the time when the matter was on the dismissal calendar, and if I recall, you made very much the same statement you made in this affidavit, now. More in the nature of a motion for re-hearing of the, or on the motion on dismissal.

Mr. O'Neill: Well, I might state, Your Honor, that I didn't have—I didn't state to the Court all the facts that are in the affidavit, or all the reasons therefor. I did mention the letter that I wrote to Mr. Woelflen. That was about the size of it, Your Honor.

I feel that the other matters that I did not at that time present to the Court, that it was through inadvertence on my part and without any intention whatever to delay the matter, Your Honor. I had no intention whatsoever of attempting to put the matter off or keep it from going to trial, or anything of that nature.

The Court: You see, Mr. O'Neill, this is an old case. The matters that were alleged to be after a couple of amended complaints were filed, the cause of action in this case, arose in 1954, four years ago. And the complaint was not filed until the very last day of the statutory period, as I recall.

Mr. O'Neill: That is correct, Your Honor.

The Court: In 1956. Now, two years have again gone by, and it has become an old case. While the statutory period, of course, may be advantaged by

a litigant in filing his suit, at the same time, if the whole period is used, and then another period of equal length of non-prosecution follows, the result is the case really becomes stale, and the Government is not in a position to get witnesses, people have to testify as to old events.

What is your position with respect to this matter?

Mr. Woelflen: Well, Your Honor, I stated my position in the past, and I realize Mr. O'Neill's position; but I have a client that I must represent, and although Mr. O'Neill stated to Your Honor this morning that this deals with conditions at the hospital, that is not necessarily the entire allegation of the complaint, because paragraph 8 of the amended complaint, at page 2, does deal with medical services and treatment of Government doctors.

So it does, in some degree, entail the services and the testimony of Government doctors.

Now, it is to date, 50 months, almost, to the date of the mal-practice, which happened on April 11, 1954, and this is June 11, 1958. So that's four years and two months from the date of this incident. Some of our doctors are no longer available.

I might state to Your Honor, what Mr. O'Neill said was correct, that in December he did call me and I said I would do something about it. During the press of my own business, I overlooked that. But still there was a lapse of four months from the time we discussed this matter until the dismissal calendar, and I think the onus sometimes shifts during that period of time.

If I had neglected, I think counsel should have called it to my attention. Nothing even was called to my attention when the notices for dismissal appeared, and those go out sometimes a week before a dismissal calendar is called. I heard nothing from Mr. O'Neill until he appeared here in Court. If there was some basis in fact for setting aside dismissal, and the facts are readily available to Mr. O'Neill subsequent to April 23rd, I feel in honesty and justice something should have been done immediately, but nothing was done again for another month.

We received this motion on the 28th of May, which was a month after the dismissal. I feel that I cannot, in good conscience, state that the Government could adequately defend this case under the circumstances.

The record will show that there were several amended complaints, several motions for a more definite statement. There was some change in theory or specifications in the charges. Up until the second amended complaint was filed on April 17, 1957, which was a year after the original complaint was filed, and three years after the incident, we were unable to specifically investigate the facts.

We have a hospital file—but to pinpoint exactly what treatment, or what operative procedures were the basis for plaintiff's complaint, we were unable to correlate that until we had the amended complaint filed.

Now, I am not critical of counsel, and I don't want to appear that way, because I know Mr.

O'Neill, and we are personal friends. But I have to take a stand on this. There was many months' lag between the time of the order for the amended complaint, and the filing of the amended complaint. I think the record discloses that. It took practically 11 months to get a responsive complaint on file. And I think Judge Hamlin granted a motion for a more definite statement—I beg your pardon; on June 23, 1956, Judge Murphy granted a motion for a more definite statement.

A first amended complaint was not filed until October 8, 1956, which is approximately two months later. On November 19, 1956, we filed another motion for a more definite statement, which was granted by Judge Hamlin on December 4, 1956.

On April 17, if it please the Court, almost five months later, the second amended complaint was filed.

Now, taking into consideration any dereliction on my part, which would begin on December of 1957, through April of this year, I still feel that there has been some inaction during this period of time, and I don't want to call Your Honor's attention to it, but I think Your Honor is completely aware and fully cognizant of the language of the Court of Appeals in Bowling versus United States, which was an affirmant of Your Honor's order for dismissal, which was granted in 1956.

It cited 231 Fed. Sec. 926, which the Court of Appeals said—The language was that the power of a trial court to discuss a case, caused where the matter has become stale by virtue of inaction by

the plaintiff, is inherent and is crystalized by the rules.

And I think Your Honor has followed that policy.

I don't like to embarrass counsel, but I find myself now in an embarrassing position. If counsel was allowed to reinstate this case, and bring it to trial within 60 or 90 days, I would have to represent to the Court we would not be in a position to bring the case to trial.

I have sat on this matter pending information from counsel. And again, we have another action—the record shows that our interrogatories were propounded on May 17, 1957, and under the rules, they are supposed to be answered within 15 days. I usually give concessions on that, but in this case, the interrogatories were not answered until August 29, 1956, which again is beyond the prescribed period.

And that information, when it came in then, we would have been in a position to go fully ahead with the matter. So Your Honor can see that when we were in a position to really go forward, it was a year and four months after the action was instituted, and approximately three years and four months after the cause of action accrued.

And I must respectfully request the Court, in deference to counsel, understanding his position, that the request for the order of dismissal of April the 23rd, stands.

Mr. O'Neill: May I just state, Your Honor, that I would like to correct Mr. Woelflen in one respect,

that when I did receive the notice in this matter, notice that this matter was on the dismissal calendar, I at that time contacted him and, for the first time, was advised the doctors were not available for deposition at that time.

I might state, Your Honor, that even had I noticed the depositions at the time of the custodian of records, at the time that I had written to Mr. Woelflen, the matter would never even have been on the calendar, because the matter would then have had action proceeding toward trial in the matter, and it was simply an inadvertence on our part that we did not take the deposition, because we were waiting to hear when the depositions could be taken.

Now, had we just noticed the deposition, the matter would never even have been on the calendar, Your Honor, and we would have been able to proceed ahead to trial.

Now, I certainly would grant any request that the Government would have in the way of preparation of this case for any purpose at all. But I do feel that the matter should have the opportunity to be heard on its merits; whether it is a meritorious case or not is, of course, one that's going to be up to the decision of the trial judge.

But I do feel that it's a case that should be heard on its merits, Your Honor.

The Court: Submitted?

Mr. Woelflen: I will stand on my prior statements.

The Court: Well, I am satisfied that the record in this case shows a substantial failure to prosecute,

bringing it in the rule for dismissal, and that there has been no showing why the order made on April 23rd for dismissal should be set aside. So the motion to set aside the order of dismissal will be denied.

[Endorsed]: Filed August 14, 1958.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, C. W. Calbreath, Clerk of the United States District Court for the Northern District of California, hereby certify the foregoing and accompanying documents, listed below, are the originals filed in this Court in the above-entitled case and constitute the supplemental record on appeal herein, as designated by counsel for the appellant:

Reporter's Transcript of Proceedings, April 23, 1958.

Reporter's Transcript of Proceedings, June 11, 1958.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court this 15th day of August, 1958.

[Seal] C. W. CALBREATH,
Clerk
/s/ By MARGARET P. BLAIR,
Deputy

[Endorsed]: No. 16110. United States Court of Appeals for the Ninth Circuit. Jerry Lee Birdsong and Dennis Birdsong, by and through their guardian ad litem, Ora Mae Birdsong, and Ora Mae Birdsong, Appellants, vs. United States of America, Appellee. Transcript of Record. Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed: July 18, 1958.

Docketed: July 24, 1958.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 16110

JERRY LEE BIRDSONG and DENNIS BIRDSONG, by and through their guardian ad litem, ORA MAE BIRDSONG, and ORA MAE BIRDSONG, Appellants,

vs.

UNITED STATES OF AMERICA,
Appellee.

STATEMENT OF POINTS AND DESIGNATION OF RECORD

Plaintiffs and appellants hereby adopt the state-

ment of points and designation of record appearing in the typed record herein.

Dated: July 22, 1958.

KAISER & O'NEILL,
/s/ By JEREMIAH F. O'NEILL, JR.,
Attorneys for Appellants

Affidavit of Service by Mail attached.

[Endorsed]: Filed July 24, 1958. Paul P. O'Brien, Clerk.

[Title of Court of Appeals and Cause.]

APPELLEE'S DESIGNATION OF RECORD

The appellee United States of America does hereby designate the entire record of the United States District Court for the Northern District of California as a record on appeal in the above matter.

Dated: July 29, 1958.

LLOYD H. BURKE,
United States Attorney
/s/ FREDERICK J. WOELFLEN,
Assistant U. S. Attorney
Attorneys for Appellee

Affidavit of Service by Mail attached.

[Endorsed]: Filed July 30, 1958. Paul P. O'Brien, Clerk.

No. 16,110

United States Court of Appeals

For the Ninth Circuit

JERRY LEE BIRDSONG and DENNIS BIRDSONG, by and through their guardian ad litem, Ora Mae Birdsong, and ORA MAE BIRDSONG, *Appellants,* vs. UNITED STATES OF AMERICA, *Appellee.*	

APPELLANTS' OPENING BRIEF.

KAISER & O'NEILL,
ROBERT A. KAISER,
JEREMIAH F. O'NEILL, JR.,
428 Thirteenth Street
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Attorneys for Appellants.

FILED
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PAUL P. O'BRIEN, Cl

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No. 16,110

United States Court of Appeals

For the Ninth Circuit

JERRY LEE BIRDSONG and DENNIS BIRDSONG, by and through their guardian ad litem, Ora Mae Birdsong, and ORA MAE BIRDSONG, *Appellants,* vs. UNITED STATES OF AMERICA, *Appellee.*	

APPELLANTS' OPENING BRIEF.

STATEMENT OF JURISDICTION.

This is an appeal from an order of the United States District Court, for the Northern District of California, Southern Division, Honorable Louis E. Goodman presiding, dismissing the within action.

The case involves an action for wrongful death alleged to have taken place in the Veteran's Hospital, located in the City of Oakland, County of Alameda, State of California, on April 11, 1954, as a result of the negligence of the agents and employees of the defendant and appellee United States of America.

The basis for the jurisdiction of the United States District Court is found in 28 U.S.C.A. 1346(b):

> Subject to the provisions of chapter 171 of this title, the district courts, together with the District Court for the Territory of Alaska, the United States District Court for the District of the Canal Zone and the District Court of the Virgin Islands, shall have exclusive jurisdiction of civil actions on claims against the United States, for money damages, accruing on and after January 1, 1945, for injury or loss of property, or personal injury or death caused by the negligence or wrongful act or omission of any employee of the government while acting within the scope of his office or employment, under circumstances where the United States, if a private person, would be liable to the claimant in accordance with the law or the place where the act of omission occurred.

The basis for the jurisdiction of the United States Court of Appeals for the 9th Circuit is found in 28 U.S.C.A. 1291:

> The courts of appeals shall have jurisdiction of appeals from all final decisions of the district courts of the United States, the District Court for the Territory of Alaska, The United States District Court for the Distict of the Canal Zone, and the District Court of the Virgin Islands, except where a direct review my be had in the Supreme Court.

STATEMENT OF THE CASE.

On April 11, 1954, Thomas William Birdsong died in the Veteran's Hospital located in the City of Oakland, County of Alameda, State of California.

Thereafter on April 10, 1956, plaintiff caused to be filed a complaint for wrongful death in the United States District Court for the Northern District of California, Southern Division. (T.R. pages 5-8.)

The Docket entries, as indicated in the transcript of record, pages 3 to 5, indicate that after the filing of the complaint various actions were taken by both parties until April 16, 1958, when the clerk of the District Court mailed notice that the matter would appear on the dismissal calendar pursuant to rule 14 of the Rules of Practice of the United States District Court for the Northern District of California.

On April 23, 1958, the Honorable Louis E. Goodman ordered the within matter dismissed for lack of prosecution. (T.R. pages 35-36.)

The question involved in this appeal is:

Did the Honorable District Court, Louis E. Goodman, presiding, err in dismissing the within cause?

SPECIFICATION OF ERRORS.

Appellant respectfully urges that the Honorable District Court erred in the following respects:

That under all the circumstances of the case it was an abuse of discretion for the Honorable Court to dismiss this case for lack of prosecution.

ARGUMENT.

Rule 14 of the Rules of Practice, United States District Court, Northern District of California, provides as follows:

> *Dismissal for Want of Prosecution*
>
> At a time fixed by the court at least every six months, the clerk in open court, under the supervision of the master calendar judge, shall call all civil actions pending in which no steps have been taken for six months.
>
> Notice of the calling shall be mailed to all attorneys of record. If none of the parties nor their attorneys appear, or if good cause for the lack of prosecution is not shown, the court may dismiss the action.

The question then is clearly presented:

Was good cause shown why no steps had been taken for six months in the within action?

Appellants earnestly and respectfully submit that good cause was indeed shown. The following facts as quoted from the affidavit of Jeremiah F. O'Neill, Jr., (T.R. pages 37-39) are uncontradicted, and indeed verified by the attorney for appellee during the proceedings on motion to set aside dismissals for lack of prosecution. (T.R. page 58.)

"That on December 17, 1957, your affiant wrote a letter to Mr. Frederick J. Woelflen, one of the attorneys for the defendant herein, requesting that depositions of the Custodian of Records of the Veteran's Administration Hospital and the doctors involved be taken, a copy of which letter is attached hereto and

incorporated herein by reference; that in said letter your affiant requested that he be advised whether the depositions could be taken by stipulation, or whether the United States Attorney's Office requests notice of depositions to be taken; that within a few days after sending the letter above referred to, your affiant received a telephone call from Mr. Woelflen to discuss the subject matter of the letter; that at said time Mr. Woelflen stated to your affiant that the defendant was willing to have the depositions taken by stipulation, but that the whereabouts of some of the doctors might not be known since the possibility existed that some of them were no longer with the Veteran's Administration Hospital; Mr. Woelflen further stated that because of this problem, it would probably take considerable time for him to locate the doctors and arrange for the taking of their depositions, and that he would contact your affiant when the same were arranged;

That relying upon the statements of Mr. Woelflen, your affiant inadvertently filed the case away, and due to the press of business, did not do anything further with reference to the taking of the depositions while waiting to hear further from Mr. Woelflen; that because of Mr. Woelflen's statement that considerable time would be necessary to contact the doctors, your affiant was not worried about the passage of time until the notification that the case would appear on the dismissal calendar; that at that time your affiant again telephoned Mr. Woelflen and was advised by him for the first time that the doctors were not available; that had your affiant known that the doctors were not

available, he would have proceeded with the deposition of the Custodian of Records of the Veteran's Administration Hospital, as well as taking investigative steps to locate the doctors;"

Mr. Woelflen himself verified the above statement. "I might state to Your Honor, what Mr. O'Neill said was correct, that in December he did call me and I said I would do something about it. During the press of my own business, I overlooked that."

It is thus clear that the reason no steps were taken during the six months immediately preceding the dismissal hearing was that appellants were assured that the doctors would be made avaliable for deposition without the necessity of formal notice; that appellee's counsel inadvertently neglected to procure the doctors for depositions; that appellants relied upon the assurances of appellee's counsel without any intent on their part to in any way delay or prolong the litigation.

Appellants realize that the general rule is that a dismissal for lack of prosecution will not be disturbed by the Appellate Court in the absence of a showing of an abuse of discretion on the part of the trial court. (*Boling v. United States,* 231 Fed. 2d 926.)

It would seem that where the delay or lack of prosecution stems from reliance by the appellants upon assurances by appellee, it is an abuse of discretion to penalize appellants therefor. Had appellants been aware that nothing was being done in the way of making the doctors available, appellants could have proceeded to take the deposition of the Custodian of

Records and the matter, having had action within six months, would never even have appeared on the dismissal calendar.

CONCLUSION.

It is respectfully submitted that the Honorable District Court erred in dismissing the within matter and appellants respectfully request that said dismissal be reversed so that the matter may be tried on its merits.

Dated, Oakland, California,
October 22, 1958.

Respectfully submitted,
KAISER & O'NEILL,
ROBERT A. KAISER,
JEREMIAH F. O'NEILL, JR.,
Attorneys for Appellants.

No. 16,110

United States Court of Appeals

For the Ninth Circuit

JERRY LEE BIRDSONG and DENNIS BIRDSONG, by and through their guardian ad litem, Ora Mae Birdsong, and ORA MAE BIRDSONG, *Appellants,* vs. UNITED STATES OF AMERICA, *Appellee.*	

BRIEF OF APPELLEE.

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No. 16,110

United States Court of Appeals

For the Ninth Circuit

JERRY LEE BIRDSONG and DENNIS BIRDSONG, by and through their guardian ad litem, Ora Mae Birdsong, and ORA MAE BIRDSONG, *Appellants,* vs. UNITED STATES OF AMERICA, *Appellee.*	

BRIEF OF APPELLEE.

STATEMENT OF THE CASE.

The appellants' statement of the case as recited in their brief is essentially correct. However, the brevity of this statement does not present to the court the true history of the litigation prior to its being dismissed by Federal Judge Louis E. Goodman on April 23, 1958.

The appellants' action for wrongful death was instituted one day prior to the running of the Statute of Limitations. 28 U.S.C. 2401. The complaint (Tr. 5 through 8) discloses that the cause of action upon which appellants based their claim occurred on April

11, 1954. The action was commenced on April 10, 1956.

A review of the docket entries (Tr. 3, 4 and 5) discloses the appellants were unable to present to the court an amended complaint which could be properly answered until one year and eight days following the filing of the original complaint. This was accomplished in the form of a Second Amended Complaint. (Tr. 17-21.)

During the first year that this case was pending in the District Court two separate motions for a more definite statement were filed by the appellee and granted. The first motion for a more definite statement was granted on July 23, 1956. (Tr. 11-12.) No first amended complaint was filed until October 9, 1956, approximately three months following the granting of the motion for a more definite statement. (Tr. 12-15.) Rule 12(a)(2) of the Federal Rules of Civil Procedure requires that an amended pleading shall be filed within 10 days after granting a motion for a more definite statement. Following the filing of the first amended complaint, the appellee again filed a motion for a more definite statement which was granted on December 4, 1956. (Tr. 16-17.) Not until April 18, 1956, more than four months after the court, for a second time, granted appellee's motion for a more definite statement was a second amended complaint filed. (Tr. 17-20.)

Subsequent to the filing of the second amended complaint, the appellee filed its answer (Tr. 21-22) and on

May 17, 1956, propounded written interrogatories to the appellants. (Tr. 22-35.) The written interrogatories were not answered by the appellant until August 29, 1957, three months after they were served, this being contrary to Rule 33 of the Federal Rules of Civil Procedure which requires that responses be made within 15 days.

SPECIFICATIONS OF ERROR.

It is the position of the appellee that the United States District Court for the Northern District of California did not abuse its judicial discretion in dismissing appellants' complaint and cause of action for lack of prosecution.

ARGUMENT.

The only authority which appellants have cited in their brief is *Boling v. United States,* 231 F. 2d 926, a decision of this Appellate Court. The facts in the *Boling* case are almost identical to the instant appeal. The Federal Judge that dismissed the *Boling* case for lack of prosecution is the same Federal Judge that dismissed this case. At the very outset of the *Boling* case, this court stated:

> "The power of the trial court to dismiss a cause where the matter has become stale by virtue of *inaction* by plaintiff is inherent and has been crystalized by rule. Rule 41(b), Federal Rules of Civil Procedure, 28 U.S.C.A. One of the causes of congestion of the trial dockets is the

> failure of courts to exercise the authority vested in them thus to dispose of cases which are shaky or unfounded but which are held on the calendar for nuisance value. Since trial judges are hesitant to dismiss such causes of their own motion, for fear of injustice to some litigant, the device of placing cases in which no action has been taken for a considerable time on a docket for dismissal, absent a showing of adequate explanation for the delay, has been used. But even this palliative for the admitted evil has been of little avail, because of the innate hesitancy mentioned above. Because of this fact, an order of dismissal for failure to prosecute *will never* be set aside unless there has been an abuse of discretion, and, of course, such a situation is not presumed." (Emphasis added.)

The main complaint upon which the appellants rely for a reversal of the order of dismissal is their attorneys' statement that they did nothing toward further prosecution of the civil litigation pending word from appellee's counsel as to the availability of certain defense witnesses for deposition. (Brief, pages 3, 4 and 5.)

It is to be noted that this reliance by appellants' counsel as to the appellee's attorney securing witnesses for a deposition continued for approximately five months. Nothing was done by appellants during this period of time. This reason for delay was thoroughly discussed before Judge Goodman on the occasion of this case's appearance on the civil dismissal calendar. This explanation of inaction was called to the court's attention again on appellants' subsequent motion to

set aside the order for dismissal. (Tr. 51, 55, 56 and 57.) It is eminently clear from the transcript and the comments of the District Judge that all the problems presently before this court were duly and thoroughly considered by Judge Goodman prior to his dismissing this action. The record does not demonstrate the exercise of gross abuse of discretion by the trial court in dismissing this case that warrants a reversal by this court.

> *Hicks v. Bekins Moving & Storage Co.*, 115 F. 2d 406 (9th Cir. 1940);
>
> *Sweeney v. Anderson,* 129 F. 2d 756 (10th Cir. 1942);
>
> *United States v. Pacific Fruit & Produce Co.,* 138 F. 2d 367 (9th Cir. 1943);
>
> *United States v. McWilliams,* 163 F. 2d 695 (D. C. Cir. 1947).

In *Boudreau v. United States,* 250 F. 2d 209, this court recently affirmed its decisions in *Boling v. United States,* supra, and *Hicks v. Bekins Moving & Storage Co.,* supra. The court in the *Boudreau* case found that the trial court properly exercised its judicial discretion in dismissing a case for want of prosecution. The same situation exists here.

It is respectfully submitted that in view of the long history of delays on the part of appellants in failing to timely file amended complaints after motions for a more definite statement were granted and appellants' failure to timely answer the appellee's interrogatories clearly disclose that the appellants were not prompt and expeditious in disposing of their litigation from

the very moment of its inception. The mere fact that they were stirred into action after being notified of a pending dismissal is no excuse for their past dereliction and not a sufficient reason to persuade a trial court to refuse to exercise its judicial power in dismissing stale and long-standing cases. *Hicks v. Bekins Moving & Storage Co.,* supra.

CONCLUSION.

The dismissal of appellants' claim against appellee was justified and a proper exercise of an inherent judicial power. Arguments propounded by the appellants fail to disclose that the District Court abused its discretion in granting this dismissal. In the absence of any showing on the part of the appellants that there was abuse of discretion, a reversal cannot be effected by this court.

The appellee respectfully submits that the order of dismissal be affirmed.

Dated, San Francisco, California,
November 5, 1958.

Respectfully submitted,

ROBERT H. SCHNACKE,
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Attorneys for Appellee.

No. 16,111

IN THE

United States Court of Appeals

For the Ninth Circuit

JOHNNIE ELMEASE MADRIGAN,
Appellant,

vs.

UNITED STATES OF AMERICA,
Appellee.

ROBERT EDWARD MADRIGAN and PATRICIA ANN MADRIGAN, by and through their guardian ad litem, Fred J. Madrigan,
Appellants,

vs.

UNITED STATES OF AMERICA,
Appellee.

On Appeal from the United States District Court for the Northern District of California, Southern Division.

BRIEF FOR APPELLANTS.

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DEC 23 1958
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No. 16,111

IN THE

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JOHNNIE ELMEASE MADRIGAN, *Appellant,* vs. UNITED STATES OF AMERICA, *Appellee.*	
ROBERT EDWARD MADRIGAN and PATRICIA ANN MADRIGAN, by and through their guardian ad litem, Fred J. Madrigan, *Appellants,* vs. UNITED STATES OF AMERICA, *Appellee.*	

On Appeal from the United States District Court for the Northern District of California, Southern Division.

BRIEF FOR APPELLANTS.

I. JURISDICTIONAL STATEMENT.

This is an appeal from a final judgment in favor of the defendant, United States of America, granted

in the United States District Court for the Northern District of California, Southern Division, the Honorable Willis W. Ritter of Utah sitting specially. The action, founded on alleged negligence and malpractice of persons for whom the defendant was legally responsible, was instituted by plaintiffs-appellants under the authority of the Federal Tort Claims Act, Title 28, U.S.C.A., Sections 1346(b) and 2674, Revised, et seq. It is upon that Act that jurisdiction of this Honorable Court is founded. The appeal proper is authorized under 28 U.S.C.A., Section 1291, notice of said appeal having been filed on May 8, 1958.

II. THE ISSUES.

Since the entire case was tried upon the theory that the United States is liable under the Tort Claims Act for its negligence in the diagnosis, treatment and care of the dependents of servicemen, once such dependents have been accepted as patients of any dispensary, or other hospital institution operated and controlled by it, we are content to eliminate this issue, if any exists, by reference to the uncontradicted testimony of Mrs. Johnnie Elmease Madrigan which established factually that she was accepted as a patient at the Alameda Naval Dispensary and, thereafter, at the United States Naval Hospital, Oak Knoll, Oakland, California (TR 19, lines 9-10, et seq.), for intermediate procedures, and finally advised to enter as an inpatient for surgery on October 29, 1951, which was

aborted by action of the defendant's agents and employees. (TR 30, lines 16-32.)

Equally clear is the established law placing responsibility on the United States, under the controlling circumstances.

United States v. Grey, 199 F. 2d 239;
Costley v. United States, 181 F. 2d 723;
Smart v. United States, 111 F. Supp. 907;
Grigalauskas v. United States, 103 F. Supp. 543.

In the *Grey* case, supra, the applicable law is set forth:

> "Having decided that there were facilities available and having accepted her as a patient, the personnel at the hospital acted within the scope of their duties or employment in treating and caring for her (plaintiff). And any negligent act or omission on their part in the discharge of such duties which proximately caused injury to plaintiff rendered the Government liable under the Tort Claims Act. *Costley v. United States,* 5 Cir., 181 F. 2d 723."

The remaining issues may be capsulized as follows:

A. When, following submission of a service dependent patient to routine pre-operative chest X-rays, and following the report of the Government's radiologist that these X-rays reflect lung pathology, most probably adult tuberculosis, is there a duty upon the Government to advise the patient within a reasonable time of the suspected condition and the necessity (under good medical standards and practices), to

initiate a series of laboratory and clinical studies for clarification of the diagnosis and control of the disease?

B. In this regard, is the error or omission, or failure to follow a prescribed course of conduct calculated to permit the completion of such X-rays, their reading and diagnosis by a competent radiologist within a usual period of one (1) day (TR 570, lines 15-25), permitting return of the X-rays to the patient's jacket in sufficient time to be observed by the physician in charge upon the return of the patient for scheduled surgery, an act of negligence, which coupled with proximate cause and damage, presents a compensable claim under the Tort Claims Act?

C. Under existing regulations charging the Commanding Officer with the duty to discover, diagnose and control infectious diseases, coupled with reasonable standards of accepted medical practice in the community within which the Government's hospital is located, is the failure to advise a patient found to have adult tuberculosis an act of negligence which, coupled with proximate cause and damages, is compensable under the Tort Claims Act?

D. Is the Government liable for acts of *omission,* as well as *commission,* under circumstances where there is a failure to advise an accepted patient of the probable existence within her lungs of pathology which, if undiagnosed with certainty as to its activity, could, and did, cause bilateral infiltration of both lungs, far advanced and active, following an insidious onset and development of symptoms?

E. If, as a direct and proximate consequence of exposure to their mother, a patient as hereinabove described, and prior to a final diagnosis of bilateral tuberculosis, far advanced, the two (2) minor children of the patient contact and develop tuberculosis, is the Government liable to these minor children if the development and spread of the disease of tuberculosis has resulted from the failure of the Government to advise the patient of its own findings relative to the suspected tuberculosis existing within the body of said patient almost four (4) years prior to its discovery by Government personnel in a far advanced, destructive form?

F. Where the great preponderance of the evidence supporting the existence of a pathological condition in the lungs of the patient in question is confirmed and verified by learned physicians and chest surgeons, one of these a Government physician who treated the patient, another the Government's employee and agent called as the Court's own witness, who diagnosed properly the pathological condition, and still another, the Government's own expert witness, is there caprice and abuse of discretion in the findings and judgment of the learned trial judge which is based almost solely upon the testimony of a single so-called conservative medical expert presented by the Government?

That such caprice or abuse of judicial discretion, if existing, is reviewable by this learned Court is clear from the language of *Sanders v. Leech,* 158 F. 2d 48, wherein (conceding that under the Federal Rules of

Civil Procedure, 52(a), 27 U.S.C.A. following Section 723, findings of fact are not usually set aside save where clearly erroneous), the Court stated:

> "It may reverse, though, under the rule (1) where the findings are without substantial evidence to support them; (2) where the court misapprehended the effect of the evidence; and (3) if, though there is evidence which if credible would be substantial, the force and effect of the testimony considered as a whole convinces that the finding is so against the great preponderance of the credible testimony that it does not reflect or represent the truth and right of the case. (Citing, *Katz Underwear v. United States* (3 Cir.), 127 F. 2d 965; *Aetna v. Kepler* (8 Cir.), 116 F. 2d 1; *Fleming v. Palmer* (1 Cir.), 123 F. 2d 749)."
>
> See also: *Williams v. United States* (5 Cir.), 252 F. 2d 887.

III. STATEMENT OF THE CASE.

Commander Fred J. Madrigan, a United States Navy officer, with seven years in the commissioned ranks as of 1951, and fifteen years as of this writing, is the husband of Johnnie Elmease Madrigan, some twenty-seven years old at the time of the occurrences under review. Together, they had two children, Patricia Ann Madrigan, born October 6, 1948, at Portsmouth, Virginia, and Robert Edward Madrigan, born in that same city on May 2, 1950.

Mrs. Madrigan regarded herself, and she was, in fact, a vigorous, healthy woman, prior to October, 1951. Apart from hospitalization for birth of the two

children and a brief hospitalization in late 1950 or early 1951, she was an active mother and Navy wife. (TR 16, lines 10-11.)

Commander Madrigan was transferred to the west coast in July, 1951. Mrs. Madrigan and the family accompanied him to Alameda, California. At this approximate time, Mrs. Madrigan became aware of a feeling of constant fatigue, and sought medical advice in the Alameda Naval Air Station Dispensary in August, 1951. After several such appointments, she was advised to submit herself to a physician at the Oak Knoll United States Naval Hospital, Oakland, California, for a complete physical examination and a determination of the medical causes for her fatigue.

Thereafter the following events transpired:

October 12, 1951:

Mrs. Madrigan was seen by Dr. R. F. Christoff, a Naval physician, who recorded the history of her then complaint and made a diagnosis of Hallux Valgus, by definition, a growth on the soles and heels of the feet, commonly known as bunions. With this diagnosis, she was referred to Dr. C. A. Mead, a Naval orthopedist at the Orthopedic Department of Oak Knoll United States Navy Hospital at Oak Knoll, which we shall hereinafter designate as the Oak Knoll Naval Hospital, for brevity.

October 24, 1951:

Dr. Mead examined the patient, and, among other things, elicited the fact that she had foot pain and

fatigue. He recommended certain surgical procedures and ordered X-rays taken *that day,* of her feet *and her chest.* These chest X-rays were a routine pre-operative procedure and, as will later be established, were of importance in determining whether any body condition existed which would contra-indicate surgical procedure. The patient was advised to return for admission to the hospital as an in-patient.

October 29, 1951:

Mrs. Madrigan, following the advice of Dr. Mead, did return to Oak Knoll Naval Hospital for the contemplated surgery and, in the company of her husband, followed the established procedure for checking in and registering as an in-patient. (TR 30, lines 19-25.) Dr. Cruise, the chief of orthopedics, after consultation with Dr. Mead, caused the patient to be advised that in his opinion, no surgery was necessary at that time. On the contrary, conservative treatment was recommended, with certain outlined home treatments and the wearing of a particular type of shoe. The X-rays of Mrs. Madrigan's feet taken October 24, 1951, were, without question, before Drs. Mead and Cruise, these having been developed, read and placed in what is described as the patient's "jacket" *prior to her return on October 29, 1951.* As will later be demonstrated, she could not have been admitted to the hospital had the chest X-rays (following prescribed and normal routine), been before the doctors making the decision on October 29, 1951. She was advised to "check back with them . . . within a month". (TR 35, lines 21-25; TR 36, line 1.) It was the con-

tention of the Government that she never returned. It was Mrs. Madrigan's position that she did, in fact, call and report her condition as improved, to an agent of the Government at the aforesaid Oak Knoll Naval Hospital, *within a month.*

It is at this point where the history of the case is beclouded by the unpredictable and unusual events touching upon the development and reading of the chest X-rays by Dr. James G. Bulgrin, radiologist at the Oak Knoll Naval Hospital. The report on these X-rays is dated *November 9, 1951,* and this report indicated that the interpretation was made, at the request of Dr. Mead (dated October 24, 1951), on *November 8, 1951.* Dr. Mead, who had ordered these X-rays on October 24, 1951, appreciated "that these two dates seem to be at variance with what I would recall as our usual procedure in the making of these films and the subsequent reporting of these films". (TR 633, lines 16-23.) That the chest X-ray was ordered pursuant to having Mrs. Madrigan admitted as a hospital patient is nowhere denied. (TR 638, lines 6-10.) The chest X-ray was never brought to the attention of Dr. Mead prior to the time Mrs. Madrigan was scheduled for surgery on October 29, 1951. (TR 640.) Had this report been brought to the attention of Dr. Mead, he would undoubtedly have brought it to the attention of the patient and advised her of the existence of pathology in her lungs. (TR 640-641.) Thus, the crucial X-ray which strongly pointed to the necessity for immediate laboratory and clinical studies, was not before the one doctor, who, though an orthopedist, would have known the meaning of

"acid fast reinfection etiology" (tuberculosis), and made the decision to advise the patient of her condition. This—in spite of the fact that the X-rays of Mrs. Madrigan's feet were before Dr. Mead in time for Mrs. Madrigan's visit to him of October 29, 1951. The more important chest X-ray was not.

As a matter of fact, this significant X-ray report was, according to the testimony of the Court's own witness, Dr. James Bulgrin (TR 571, lines 20-22), *not read until November 8, 1951, and a report not typed until November 9, 1951.*

Within a month of the visit of October 29, 1951, Mrs. Madrigan telephoned the Oak Knoll Naval Hospital and in that telephone conversation, Mrs. Madrigan stated that "there was no mention to return to the hospital, but if they (her feet) gave me any more trouble, to let them know". (TR 39, lines 3 and 4.) Nothing was said to Mrs. Madrigan at that time regarding the X-rays of her chest which by that time had been read by Dr. Bulgrin.

Mrs. Madrigan remained in the Alameda area throughout the balance of 1951, 1952 and the first half of 1953. In that period of time, Mrs. Madrigan visited the Naval Air Station Dispensary in Alameda for an attack of sinus, but at no time was she apprised of the X-ray reading, indicating the presence of pathology.

In September, 1953, her husband having been transferred to Japan by the Navy, Mrs. Madrigan prepared to join him in that country.

Her first move was to Honolulu, Territory of Hawaii. Up to the time of this move, no chest X-rays were taken subsequent to the X-rays of October 24, 1951.

A cursory physical examination given to Naval dependents heading overseas was made in Honolulu. Again, *no chest X-rays were taken,* and still Mrs. Madrigan had no knowledge of the possibility that she might have tuberculosis.

She arrived in Yokohama, Japan, in the company of her children in October of 1953. After six weeks in Yokohama with her husband, the entire family moved to Minamiku, and in the summer of 1954, the family moved once again to "Area X", Yokohama, Japan. In May of 1954, Mrs. Madrigan was admitted to Army Hospital #8168, Yokohama, because of severe emotional problems which beset her. We feel secure in suggesting that even then, the disease was taking its toll.

She continued to demonstrate the insidious outcroppings of tuberculosis and she became increasingly nervous and more burdensome, causing her to become irritable, with a tendency towards over-indulgence in alcoholic beverages.

In May of 1955, this physical and mental state having continued without diminution, Mrs. Madrigan resolved to go to the U. S. Naval Hospital #3923, determined to find definite medical clarification of her persistent and accumulating symptoms.

She was admitted to U. S. Naval Hospital #3923 on *May 13, 1955,* at Yokohama. The diagnosis con-

firmed at that hospital was: "tuberculosis pulmonary, far advanced". (TR 58, line 12.)

This was the first time that Mrs. Madrigan ever knew that she had been suffering from tuberculosis. (TR 60, lines 5-9.)

Following that diagnosis, Mrs. Madrigan remained at the last described hospital in Yokohama for approximately two weeks, and was thence repatriated, first to Trippler Hospital in Hawaii, then to U. S. Naval Hospital, Oak Knoll, Oakland, California, from May 28, 1955, to June 13, 1955, then to Fitzsimmons Hospital in Denver. On November 1, 1955, she was transferred to Parks A.F.B. Hospital, California, where she was a tubercular in-patient until March 2, 1956, when she was given the status of an out-patient, which continues to this date.

Due to the naturally close contact between mother and children, and the well-known communicability of tuberculosis, Mrs. Madrigan's children, Robert Edward Madrigan and Patricia Ann Madrigan, were tested for tuberculosis on June 28, 1955, at Letterman Army Hospital in San Francisco, California (to which they had been returned from Japan).

Patricia Ann Madrigan, 7½ years of age, was found to have a "positive tuberculin" (TR 234, line 23) which indicates the presence of tuberculosis organisms in the body.

Robert Edward Madrigan, Mrs. Madrigan's 5-year-old son, was found to have "pulmonary infiltrate", which is considered to be primary tuberculosis. The boy was kept out of school for two months, and, al-

though his physical condition has now improved, his exposure to his mother's tuberculosis has committed him for the rest of his life to constant care and, in the foreseeable future, to semiannual physical examinations. (TR 234 through 237.)

IV. APPLICABILITY OF THE SEVERAL STATE AND FEDERAL LAWS.

We address ourselves briefly to a consideration of applicable law, arising from the laws of the State of California, within which the incidents have occurred, and such Federal law regulations and statutes as may herein be relevant.

A. The Liability of the Government Is Determined by the Substantive Law of the State of California.

Under the Tort Claims Act (supra), the United States is liable in the same manner and to the same extent as a private individual under like circumstances.

28 U.S.C.A., Section 2674. (Rev.)

B. An Action for Negligence of a Hospital or Doctor (Malpractice) May Be Maintained Under the Laws of the State of California.

Under California law the physician and surgeon, in undertaking professional service to a patient, impliedly represents that he possesses that degree of learning and skill ordinarily possessed by physicians and surgeons of good standing practicing in the same

locality. This is, of course, equally true of hospitals and like institutions.

McCurdy v. Hatfield (1947), 30 C. 2d 492;
Lawless v. Callaway (1944), 24 C. 2d 80.

It is his duty to use the care ordinarily exercised in like cases by reputable members of his profession, practicing in the same locality; to use reasonable diligence and his best judgment in the exercise of his learning, in an effort to accomplish the purpose for which he is employed. A violation of those duties is a form of negligence characterized as malpractice. Malpractice sounds in tort.

Costa v. Regents of the U. of California (1953), 116 C.A. 2d 445.

The California Health and Safety Code, Section 2571, defines tuberculosis as a communicable disease and in Section 2573, imposes the following obligations:

> "All physicians, nurses . . . shall promptly report that fact (tuberculosis) to the Health officer, together with the name of the person, the place where he is confined and the nature of the disease, if known."

C. Navy Medical Regulations Required Early Detection, Supervision and Treatment of All Tubercular Patients.

Bureau of Medicine, Department of the Navy, "General Physicians", Chapter 22, Communicable Disease Control, Section 7, subdivision 1(c) in its relevant parts reads as follows:

> "The medical officer shall be responsible for the following: Individuals suspected of having active

tuberculosis shall be admitted to the sick list and infection precautions taken until the disability is found not to exist or the disease is determined to be inactive or arrested." (TR 664, 665.)

"The medical officer shall be on the alert for early detection of infectious diseases, shall recommend the necessary control measures to the commanding officer, and shall institute the necessary restrictions of personnel and take such other action with the approval of the commanding officer as may be required to prevent the spread of communicable disease." (TR 665, lines 15-23.)

Prior to the embarkation of Mrs. Madrigan, Navy regulations required the following:

"Navy examination at the port of embarkation shall be sufficiently complete to determine the fitness of the individual to undertake the voyage in a passenger status and *to detect the presence of an infectious disease.* Results shall be recorded on the back of the certificate and shall be forwarded if cleared for travel to the medical officer responsible for the care of such persons during travel." (TR 667, lines 17-25.)[1]

D. The Government Acknowledged and Admitted Its Basic Responsibility to Advise Patients of Abnormal Conditions in Chest X-rays.

The Government admitted in answers to plaintiffs' interrogatories eight and thirty-two that there were

---

[1]In view of these strict requirements the cursory, almost indifferent examination, without requiring chest X-ray which would have conceivably alerted the authorities is almost shocking. The ONLY comment on her embarkation certificate is "OKAY". (TR 668, lines 10-14.) Counsel for the Government himself confirmed this fact!

prescribed procedures, regulations and requirements that a patient be advised of the diagnostic findings of tests, X-rays and examinations to which such patient had submitted herself and that these were in existence in 1951. (TR 759.)

Further, that during October, 1951, regulations and directives of the Navy Department and/or the Bureau of Medicine and Surgery, and accepted medical practice required follow-up procedures and treatment in cases demonstrating abnormal conditions disclosed in chest X-rays. (TR 759.)

E. The Government Is Liable for Acts of Omission as Well as Commission of Its Agents and Officers Acting Within the Scope of Their Authority.

We have urged in part that the failure of the defendant to advise, forewarn and alert plaintiff, Mrs. Madrigan, to the existence of pathology in her chest, resulted from an act of omission, i.e., failure to follow prescribed, routine, *usual and accepted standards of conduct.*

In the *Grey* case (supra), the Court stated:

> ". . . And any negligent act or omission on their part in the discharge of such duties which proximately caused the injury to plaintiff rendered the Government liable under the Tort Claims Act."

In *Costley v. United States,* 181 F. 2d 723 at 724, the Court's language is relevant:

> "Under the Tort Claims Act, the United States may be liable for money damages for injury . . . caused by the negligent or wrongful act *or omis-*

sion of any employee of the government while acting within the scope of his office . . ."

We feel there can be no serious contention regarding the existence of the Governmental DUTY in the case at bar, and face the problems of dereliction, proximate cause and resulting damage as we turn to our argument.

V. WE ARGUE OUR CASE.

A. THE X-RAYS OF OCTOBER 24, 1951, WERE PATHOLOGICAL, REFLECTING THE PRESENCE OF DISEASE.

The learned and well qualified Dr. Sidney J. Shipman, presented as a witness for the Government, offered the following under cross-examination:

"Q. Is there pathology as you view the X-ray of October 24, 1951?

A. Yes, there is." (TR 393, lines 21-23.)

We addressed question to Dr. Horton Corwin Hinshaw at page 523 of the transcript:

"Q. Would a person with lesions of the sort shown in the October, 1951 X-ray be a person then who could be stated to be 'free from infectious disease'?

A. No."

Dr. Roger Wilson, an eminent chest surgeon, examined the X-ray of October 24, 1951, found it of good quality and diagnostic. (TR 188 et seq.) He reviewed it in its entirety for the Court, indicating the areas of abnormality. His attention was directed to

the interpretation of Dr. James Bulgrin, the Navy radiologist. He agreed with it. It stated:

> "Impression: minimal fibrotic appearing infiltration left upper lung. Acid fast reinfection etiology must be considered first."
>
> "Q. Will you describe to us in simple language what this means?
>
> A. It means that the radiologist saw the opacity that I have pointed out in the left upper part of the X-ray of the lungs. 'Acid fast etiology' is a term used for *tuberculosis* in case the patient should see the record and be alarmed and 'acid fast' is colloquialism used by physicians.
>
> Q. Meaning——
>
> A. *MEANING TUBERCULOSIS.*" (Emphasis added.) (TR 214, et seq.)

Although the record is replete with medical testimony directed to this same effect, time and space require curtailment.

The Navy radiologist, Dr. James Bulgrin, was firm in his interpretation of the X-ray of October 24, 1951. He affirmed the medical significance of "acid fast etiology". (TR 586, et seq.)

> "Q. Now, when you use the term 'acid fast reinfection etiology must be considered first', what do you mean sir——
>
> A. I MEAN ADULT TUBERCULOSIS." (Emphasis added.)
>
> Q. That is a polite way of saying it, isn't it?
>
> A. Yes."

Dr. Bulgrin continued showing the reason for the use of this language and added:

"A. . . . It may be true that this is not tuberculosis. *The odds are overwhelming in favor that it is,* but that is not a certain diagnosis of tuberculosis.

Q. But the odds are overwhelming that it is.

A. Yes."

B. THERE WAS DEVIATION FROM THE NORMAL, USUAL PROCEDURES FOLLOWED IN THE GOVERNMENT'S HOSPITAL FOR THE READING, INTERPRETATION AND ACTION UPON THE OCTOBER X-RAYS.

(1) The X-ray of October 24, 1951 Required Action.

The basic question was not whether the lesions observed in the X-ray of October 24, 1951 were actually those of tuberculosis. The lesions were pathological. The evidence was strong in favor of tuberculosis. The X-rays of the feet *and chest* were ordered on October 24, 1951. The patient submitted herself on that same day. Ordinarily, following the routine at Oak Knoll Naval Hospital X-rays were ready for reading the day taken or the next day. (TR 570, lines 15-25, and 571.)

The X-rays of Mrs. Madrigan's feet were actually taken on October 24, 1951, and read and interpreted *that same day.* (TR 610.) They were present in her "jacket" and available to Dr. Mead and Dr. Cruise in the orthopedic department on October 29, 1951 when Mrs. Madrigan presented herself for admission as an in-patient for surgery. *The chest X-rays were not there.*

Had the defendant's own routine procedures been followed, then with reasonable certainty and consistent

with good practice, they would have been noted and should have been noted by Drs. Mead and Cruise, who, although orthopedists, would understand the implications of Dr. Bulgrin's interpretation.

Dr. Mead, testifying by deposition, was asked (TR 640, line 25; TR 641, lines 1-3):

> "Q. Had this report been brought to your attention you would have called it to the attention of the patient; would you not, Doctor?
>
> A. Yes, sir."

Dr. Shipman, the Government's learned expert, had this view of the problem (TR 410-418):

> "Q. . . . if you in private practice, or if you in a hospital had attended a patient, and came across a chest X-ray like this, the one in 1951 . . . if you saw anything that that woman needed, follow-up care, further treatment, further X-rays, further tests, you certainly would have gone out and got her and brought her in—sent for her and have seen she was there?
>
> A. *Yes, certainly.*" (Emphasis added.)

Dr. Horton Corwin Hinshaw, upon whose testimony the Court seemed to rely almost exclusively in its decision, faced the problem in this manner:

> "Q. Doctor, with regard to the pathology shown and with regard to Dr. Bulgrin's report thereon, would you, sir, having that X-ray in mind, and Dr. Bulgrin's reading before you, permit it to sit without further action, or would you feel that it required further investigation, further concern on the part of the doctor, for his patient?
>
> A. Yes.

Q. You feel it would?

A. That it would require further investigation, yes."

C. THE FAILURE TO HAVE THE CHEST X-RAY IN THE PATIENT'S JACKET ON OCTOBER 29, 1951, WAS DUE TO ERROR, OMISSION—NEGLIGENCE OF THE GOVERNMENT!

The Government, and in equal measure, the honorable trial judge, attempted to find some explanation for the "missing" X-ray of the chest, in the increased activity of the Korean War. Dr. Mead, her last treating doctor, would have none of it. What he did say was this (TR 642, lines 13-19):

> "*I don't think it is conceivable,* regardless of the work load that was there at that time, and knowing the efficiency of the X-ray department that an X-ray could have been taken on October 24th and not reported until November 8th or November 9th. There may have been a lag of one or two days in reporting the X-ray, but they usually got the report to us out of the X-ray department very quickly." (Emphasis added.)

Mrs. Madrigan's chest X-ray, was a routine, prescribed, pre-operative procedure. By any reasonable standard of good medical practice, that X-ray should have been in her jacket when she arrived for surgery on *October 29, 1951.* The mechanics, the instrumentalities behind the delay in this regard were in the exclusive control of persons for whom the Government is liable. We do not feel it our burden to isolate a particular individual who caused the deviation from the normal routines of the Government's hos-

pital. The deviation was caused by the error or omission of such a person. It was plain negligence and carelessness which deprived Mrs. Madrigan of the knowledge of her condition. (TR 570 et seq.)

Dr. Bulgrin, the radiologist, after advising that normally the X-ray was read the "next day", was asked for his explanation for the delay in the reading of the chest X-ray on *November 8, 1951* and the report of *November 9, 1951.*

> "Q. Your attention is invited to the fact, sir, that it (the chest X-ray) is dated November 9, 1951, on the upper left, and that the reading by yourself, sir, is dated November 8, 1951. Now, that's rather unusual, or was unusual under the system you were following at that time, wasn't it, Doctor?
>
> A. THAT'S AN ERROR OF SOME KIND, and I don't know how it came about. . . ." (Emphasis added.) (TR 572, lines 13-17.)

Dr. Mead could have sent a corpsman for the chest X-rays if they were not in the patient's file. There is no explanation by the Government, short of speculation, as to what delayed the chest X-ray under their exclusive control. Dr. Bulgrin appreciated that the chest X-ray was pre-operative and that under the usual, normal routine procedures of the hospital, the X-rays would "all then go back to the attention of the doctor so requesting them prior to the time that surgery was actually commenced." (TR 619.)

D. EVERY MEDICAL EXPERT AGREED THAT GOOD MEDICAL PRACTICE REQUIRED IMMEDIATE FOLLOW-UP LABORATORY TESTS, CLINICAL OBSERVATIONS AND CONFIRMATION OF DIAGNOSIS.

Tuberculosis is an insidious disease. Its early indications must be recognized for containment of the disease. Whether a lesion is tubercular, cancerous or otherwise potentially infectious and disabling can only be decided medically by prescribed, recognized and approved procedures. None of the experts quarreled with this basic concept. (TR 512, 513.) Dr. H. C. Hinshaw, after admitting that the chest X-ray of October 24, 1951 showed a "possible pathologic situation", was questioned as follows:

> "Q. You would, as a competent man in your field, want to rule out not only the *probability* of a lesion, the significant and potentially symptomatic, but also the possibility, would you not, sir?
> A. Yes.
> Q. And that would be good practice?
> A. Yes.
> Q. Universally?
> A. Yes." (Emphasis added.)

Dr. Bulgrin "was to be congratulated for having reported it. He obviously was looking at it very carefully", agreed Doctor Hinshaw.

We shall not belabor the record with cumulative extracts of testimony, save to assure the Court that the transcript reflects complete, unequivocal agreement of Doctors Kruisheer, Wilson, Shipman and Bulgrin that sound medical practice, in fact, common sense, would dictate follow-up procedures, tests and

clinical observations for further diagnosis and containment of the disease. Dr. Kruisheer tells us when tuberculosis was suspected at Parks Air Force Base, "We bodily send after them I mean" (TR 337, line 4), and the same procedure applies to dependents. Every suspected case of tuberculosis is reported. (TR 338, lines 3-4.) Could anything less be acceptable in view of the paternal concern of the Government for its servicemen and their dependents? Would anything less meet the requirements of good medical practice? We think not.

E. PLAINTIFF JOHNNIE ELMEASE MADRIGAN LED A HAPPY, HEALTHY, NORMAL LIFE WITH HER HUSBAND AND FAMILY UP TO 1951.

In 1951, a happy normal life was being observed by the Madrigan family. If they had disagreements, they were of a minor, quickly forgotten kind, common to any family. Because of her husband's position in the United States Navy, the Madrigans had to entertain, and were entertained frequently—but nowhere is there the slightest evidence, and all of the proof is to the contrary, that even up to 1953, Mrs. Madrigan was nothing more than a purely social drinker. Certainly she was not a compulsive one.

From 1951 to 1953, we see a gradual breakdown of this happy state of affairs.

Fatigue, irritability, family unpleasantness, and finally alcoholism itself, crept into Mrs. Madrigan's life.

Dr. Wilson reported his clinical history received from Mrs. Madrigan in these terms:

> ". . . She was just fatigued, upset, couldn't cope with things, found herself taking a nip too often in the morning time; life was just more than she could tolerate." (TR 256, lines 24-25; TR 257, line 1.)

What was the cause of these conditions?

F. TUBERCULOSIS IS INSIDIOUS AND MAY BE POTENTIALLY LETHAL DESPITE ABSENCE OF SO-CALLED CLASSICAL SYMPTOMS.

We cannot account for the Government's failure to X-ray Mrs. Madrigan in the years between 1951 and May, 1955; nor for her failure to exhibit the so-called "common" symptoms of tuberculosis, such as fever, weight loss, night sweats and the like.

But we can turn to *Diseases of the Chest,* a well known work by Dr. Hinshaw, the Government's principal witness, and the witness in whom the trial Court placed the greatest confidence, for an explanation (TR 526, 527, 528):

> "Severe and progressive pulmonary tuberculosis sometimes fails to produce any symptom which could be recognized by either the patient or his physician. Potentially lethal tuberculosis is compatible with apparent good health for a prolonged period. This failure to produce symptoms makes tuberculosis a treacherous disease which still claims victims in civilized health conscious communities. It would be a great advance if in tu-

berculosis control, every physician were aware that this disease may exist in an active form in persons without complaint, and that if symptoms are awaited, it may be in an incurable stage.

"Even though patients with advancing pulmonary tuberculosis may have no complaints referable to the lungs, they frequently have *general symptoms of indefinite character, nervous instability, excessive fatigue, vague abdominal discomforts, and other complaints indistinguishable from psychoneurosis, are common, and often attributed to unfavorable life situations.*

". . . When *symptoms are complained of* they commonly include fever, weight loss, night sweats, and other evidence of chronic infection. *Too frequently these are symptoms of overwhelming disease neglected for many months and extremely difficult to cure.*" (Emphasis added.)

And Dr. Wilson stated that he has:

". . . Seen patients with very far advanced destruction of lung who do not have symptoms and who do not lose weight and this is not an exceptional thing . . ." (TR 256, lines 10-13.)

The deterioration of Mrs. Madrigan's happiness and peace of mind were manifestations of a slow, but relentless infection with tuberculosis—which could have been checked and controlled in its early stages—but was not!

G. THE CREDIBLE MEDICAL TESTIMONY ESTABLISHES A CAUSAL RELATIONSHIP BETWEEN THE PATHOLOGY IN THE X-RAYS OF OCTOBER 24, 1951, AND THE ADVANCED INFECTIOUS PROCESS DIAGNOSED IN THE SPRING OF 1955.

1. The Great Weight of Medical Testimony Substantiates Mrs. Madrigan's Attack of May, 1955, as a Progressive Disease Having Its Origins in 1951.

Dr. Shipman, a *Government witness,* testified that in his opinion, the first evidence of tuberculosis "as far as the record goes, apparently was October 12 (sic) *1951* when a routine film was taken at the U. S. Naval Hospital in Oakland, California. Then nothing definite shows up until she was examined in Japan in 1955 when she was told she had T.B. *She had some tuberculosis during that entire period . . .*" (Emphasis added.) (TR 387.)

For emphasis, may we call this Honorable Court's attention to the following exchange between counsel and Dr. Shipman (TR 394, lines 23-25; TR 395, lines 1-5):

> "Q. Do I understand you to say, sir, that this was a continuing process from at least 1951 until the diagnosis was made in 1955, Doctor?
>
> A. That's right, yes.
>
> Q. And that there is then a definite relationship between the X-ray of 1951 and its findings and the findings in 1955, sir?
>
> A. *That's correct, yes.*" (Emphasis added.)

Then Dr. Kruisheer, member of the Department of Chest Diseases, Parks Air Force Base, told the Court (TR 323):

> "I believe that very much of the misery later on could have been prevented, and that lots of the costs of the disease later on could have been saved because I believe with reasonable certainty that the *etiology* of this lesion could have been established had there been the generally accepted method of investigation and establishing of diagnosis." (Emphasis added.)

And he added:

> ". . . and I strongly believe that indeed she (Mrs. Madrigan) had pulmonary tuberculosis, minimal active, in 1951, *which progressed to its final form* in 1955." (Emphasis added.) (TR 324, lines 17-19.)

To which Dr. Wilson added, in response to the question as to whether or not Mrs. Madrigan's disease process was a progressive thing, extending from 1951 to 1955:

> "In my opinion, this was a progressive thing." (TR 204, line 21.)

2. The Medical Testimony Is Also Overwhelming in Relating the Areas of Infection in Mrs. Madrigan's Lungs in 1955 to Those Shown in the X-ray of 1951.

Medical testimony throughout the course of the trial clearly pointed out that the "Acid fast reinfection etiology" (TR 214 et seq.), reported in the X-ray of October 24, 1951, was the area actually infected in May, 1955.

In support of this contention, we turn to the United States' most positive witness, Dr. Hinshaw, who, while

refusing to state whether or not Mrs. Madrigan actually *had* tuberculosis in *1951, does state that the areas of cavitation in 1955 were close and proximate to the site of the first suspected lesion, or that some of the cavities are in that general region.* (TR 546.)

Dr. Wilson says that he sees a definite relationship between the condition exhibited in the 1951 and the 1955 X-rays, and elaborates on the areas of involvement:

> "The later X-rays which I have seen show improvement of the same areas plus further involvement elsewhere in the lung . . . We see the same areas involved in the first and second anterior interspace . . ." (TR 201, lines 11-13; TR 202, lines 1-2.)

And, again under cross-examination by Government counsel, Dr. Wilson says:

> "In this case I think we can establish that the whole of the left upper part of the lung was involved in the 1955 disease, so the precise part of the projection in which the 1951 area was noticed must be part of that total 1955 disease.
>
> Q. But can you be sure that the whole upper part of her left lung was involved in 1955?
>
> A. I think we can, yes." (TR 279.)

And, if we may return to the testimony of Dr. Shipman, who, after comparing the report of Mrs. Madrigan's X-ray of 1951 (TR 382) and her X-rays of 1955 (TR 386), states, in answer to a *specific question* by counsel as to whether there was a "definite relationship" between the two X-rays, replies:

"*That's correct, yes.*" (Emphasis added.) (TR 395, line 5.)

We feel that this testimony, given by highly reputable men in the field of chest diseases today, irrefutably establishes a direct, proximate, and unbroken line of causation between the pathology revealed in the X-rays taken at the Oak Knoll Naval Hospital on October 24, 1951, and the acute infection with tuberculosis which was discovered in 1955.

We contend that no intervening force broke this chain of causation.

We feel that the evidence in support of our position speaks for itself, adequately and fully.

H. INASMUCH AS CHILDREN OF PRE-SCHOOL AGE ARE PRIMARILY IN CONTACT WITH THEIR PARENTS, LOGIC DICTATES, AND MEDICAL TESTIMONY SUPPORTS THE PROPOSITION THAT MRS. MADRIGAN WAS THE SOURCE OF THE INFECTION WITH TUBERCULOSIS OF PATRICIA AND ROBERT MADRIGAN.

It is well recognized that tuberculosis is an extremely infectious disease, and that close contact with an infected person required preventive precautions. (TR 664, 665, citing Navy Department precautions; see also California Health and Safety Code, Secs. 2571 and 2573.)

And Dr. Hinshaw, in his testimony, stated:

> ". . . A tuberculous mother very readily transmits the disease to her children by the very na-

ture of their intimate and oft repeated contact. It's quite unusual indeed to find a lady with tuberculosis whose children are tuberculin negative." (TR 446, lines 9-13.)

Further testimony reveals that upon discovery of the infection in Mrs. Madrigan, the maid as well as Commander Madrigan were tested, and to quote from the transcript:

> "Q. And that only the mother had it?
> A. (Dr. Wilson.) *She would then be the most likely source.*" (Emphasis added.) (TR 240, lines 14-15.)

From this testimony, we conclude that the tuberculosis infection discovered in both Madrigan children, was transmitted to them by their mother, and was the proximate result of the negligence of the staff of Oak Knoll Naval Hospital in failing to take proper and adequate steps to control this disease in 1951, when it was merely a "minimal infiltration", but nevertheless an *apparent* one!

I. DAMAGES.

As a dependent, Mrs. Madrigan was furnished the care of physicians without charge. However, there were actual costs, directly connected with her injury which are itemized below, together with such expense,

past and future, established by the evidence, covering the several plaintiffs.[2]

Mrs. Madrigan had a life expectancy of 40.28 years in 1958, being then of the age of thirty-five years. (TR 374-375.)

---

[2]*Mrs. Madrigan's* special damages are as follows:

(1) Deductions from Commander Madrigan's Navy pay were $1.75 per day (90¢ for food; 85¢ for drugs and medication) from May 13, 1955 to March 5, 1956.

This involved a total of 298 days or an overall deduction of **$521.50**

(2) Sundry expenses were incurred by Commander and Mrs. Madrigan upon their return from Japan in 1955, which included travel, telephone calls, etc.

The total involved was stated to be..... **$200.00**
(TR 647.)

(3) Future expenses, as estimated by Dr. Wilson (Tr. 229, lines 18-20), involving X-rays, office visits to physicians, etc. will be at least **$2,000.00**

Thus, the total, actual and foreseeable medical expenses for Mrs. Madrigan total **$2,721.50**

Patricia Ann Madrigan's special damages are as follows:

Mrs. Madrigan's daughter, presently 10 years of age, was placed in a private boarding school (St. Catherine's Academy, Benicia, California) for a period of eight months during her mother's hospitalization.

Her residence at the school lasted from approximately July 1955 until March 10, 1956 at a cost to Commander Madrigan of $85.00 per month, or a total cost of..... **$680.00**

Her estimated future preventive medical care, including X-rays and office visits, and assuming a life expectancy of a total of sixty-five years, will approximate $20.00 per year for fifty-five years, or **$1,100.00**

Robert Edward Madrigan's special damages are as follows:

Mrs. Madrigan's 8 year old son also was placed in St. Catherine's Academy, a month later than his sister.

Charges attributable to his residency were..... **$595.00**

His estimated future curative and preventive medical care, including X-rays and office visits and assuming a life expectancy of a total of sixty-five years, will approximate $20.00 per year for fifty-seven years, or **$1,140.00**

Total damages attributable to the Madrigan children: **$3,515.00**

Total special damages are calculated to be..... **$6,236.50**

We leave for some future day the determination of a monetary evaluation of Mrs. Madrigan's pain, suffering, embarrassment and humiliation.

She has a function loss of approximately 20 to 30% in both lungs, and we have been advised that statistically there is a 30% chance of her having a breakdown in the future. (TR 335.)

Although her disease is not active, she will have to be observed over the years, prescribed for and be acutely conscious of avoiding emotional and other disturbances which could affect a recurrence.

VI. CONCLUSION.

The learned judge below was critical of Dr. Wilson's characterization of the sequelae of tubercular infection as "horrible". He was much more impressed with the "conservative tones" of Dr. Hinshaw's commentaries which ultimately were to extricate the Government from liability. It was Dr. Hinshaw who described the disease in even stronger language as *"potentially lethal"*. (TR 526, 527, 528.)

The distinguished jurist's summation, below, with which we must respectfully disagree, could find no negligence by any person for whom the Government was responsible.

Was it not true that Dr. Bulgrin did his job well? He came up with the most probable diagnosis—tuberculosis.

Then what? The X-rays of the patient's *feet* were routed so that they got where they were supposed to be—in her jacket, and to the attention of Drs. Mead and Cruise on *October 29, 1951.*

Where were the chest X-rays with a red danger flag attached literally shouting for attention? "Hear this, Doctor, your patient most probably is tubercular!"

But Drs. Mead and Cruise never got to see the chest X-ray or the report of a potentially lethal disease. Why?

The honorable trial judge says any number of things *could* have happened. The Navy folks were busy. The X-ray could have been misplaced, lost in the shuffle, misrouted—one could speculate ad infinitum. Dr. Bulgrin did his job. Drs. Mead and Cruise were interested in her feet, contended the Government. All this while every consideration of this transcript must convince that were the chest X-ray where it was supposed to be (prior to the appearance of the plaintiff *for surgery* on October 29, 1951), these Orthopedists—physicians, if your Honors please—unquestionably would have understood the simple medical description of tuberculosis.

There is not a scintilla of evidence that had plaintiff returned physically, i.e., "returned in one month"—that even then the X-ray would have been noticed by anyone. Dr. Mead had departed for other duties by *November 29, 1951.* Where the X-ray was until it became an exhibit in the case is still shrouded in mystery.

It was from this small hole in the dike that the accumulated waters finally burst. A fair view of Mrs. Madrigan's life between 1951 and 1955, *and* thereafter through the torturesome, lonely days of treatment,

care and concern of doctors like Captain Kruisheer, until the disease was arrested, will disclose the tremendous price paid by the Madrigans—a good Navy family.

The duty and dereliction of the Government are, if we may borrow an expression, as clear and convincing as the chest X-ray of October 24, 1951. The failure to advise and alert the patient to her disease is almost inconceivable under any decent standard of due care.

The Government dereliction was the most probable cause of the development of the insidious disease through varied patterns and symptoms until the final collapse of the patient.

Were the Madrigans damaged? The Government permitted Mrs. Madrigan to depart for a foreign country with the cryptic comment—"okay". In this manner was she examined for a potentially infectious disease! Her suffering, loss of confidence, deterioration of personality and living habits are clearly part of the cycle which for a prolonged period deprived her of the fundamental right to live her early life in reasonably good health and happiness.

The two Madrigan youngsters certainly had an inherent right to be free from acquiring this disease by contact with their infected mother.

Commander Madrigan, dependent upon Naval hospitals, institutions and physicians for the continued good health of his family, had a right reasonably to anticipate that were any member of his family in-

fected and the evidence of the infection made clear to Government medical personnel, that his Government would, following prescribed procedures, routines, regulations and law, diagnose the disease with medical certainty and undertake such course of treatment and continued observation as would produce healing and containment of the disease.

It would be a tantalizing travesty on justice if now the Government were permitted to exculpate itself by the simple device of some conjecture as to why this highly volatile and diagnostically sound X-ray and its interpretation was ignored by the person responsible for its control. Though we know not who these persons may have been, we are encouraged by the language of the Court in *Seneris v. Haas,* 45 C. 2d 811, in our belief that no such specific proof was necessary. Herein the Court, describing the nature and method of proof of malpractice, said the following:

> "Generally speaking, direct and positive testimony to specific acts of negligence is not required to establish it. Circumstantial evidence is sufficient either alone or in combination with direct evidence. Circumstantial evidence may contradict and overcome direct and positive testimony. The limitation on its use is that the inference drawn must be reasonable; but there is no requirement that the circumstances to justify the inferences sought negative every other positive or possible conclusion. The law is not so exacting that it requires proof of negligence or causation by testimony so clear that it excludes every other speculative theory."

See also *Christy v. Callahan,* 124 F. 2d 825, 827.

Respectfully do we urge the Court to reverse the findings of fact made by the learned trial judge and his conclusions regarding the law which followed, upon the authorities hereinabove cited. We cannot conscientiously agree that the evidence would sustain alternative findings. We feel it points unerringly to a judgment for the plaintiffs.

Dated, San Francisco, California,
December 15, 1958.

Respectfully submitted,
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No. 16111

IN THE

United States Court of Appeals For the Ninth Circuit

JOHNNIE ELMEASE MADRIGAN, ET AL., *Appellants*

v.

UNITED STATES OF AMERICA, *Appellee*

On Appeal From the United States District Court for the Northern District of California

BRIEF AND APPENDIX FOR APPELLEE

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BRIEF AND APPENDIX FOR APPELLEE

COUNTERSTATEMENT OF THE CASE

This is an appeal from a judgment of the District Court (Judge Ritter of Utah sitting specially), denying appellants' claims against the United States under the Federal Tort Claims Act. The pertinent facts, as found by the trial court, are summarized below.

On May 13, 1955, Johnnie Elmease Madrigan, as the dependant wife of Commander Fred J. Madrigan, was admitted to a United States Naval Hospital in Japan. Subsequent medical diagnosis of Mrs. Madrigan disclosed that she had "tuberculosis, pulmonary, bilateral, active [and] for advanced (App. 4a).[1]

[1] In absence of a printed record, for convenient reference, we have set out as an Appendix to this Brief (pp. 1a-19a) the Findings of Fact and Conclusions of Law and Judgment filed by the District Court and the courts oral opinion which appears at pages 833-848 of the Reporter's transcript of the trial proceedings.

Based upon events which transpired in 1951 and which allegedly disclosed negligence by medical personnel in the Naval Hospital in California, this suit was brought by Mrs. Madrigan, under the Federal Tort Claims Act[2] in an attempt to fasten the United States with tort liability for her tubercular condition.[3]

On October 12, 1951, Mrs. Madrigan reported as an out-patient to the out-patient clinic of the United States Naval Hospital at Oakland, California. Her complaints on October 12, 1951 were "of very painful feet and fatigue" (App. 2a). Mrs. Madrigan was examined by Dr. Robert F. Christoph, a naval medical officer, who gave a diagnosis of foot deformity known as "hallux valgus" and referred Mrs. Madrigan to the orthopedic section of the out-patient clinic (App. 2a).

Mrs. Madrigan was seen on October 24, 1951, as an out-patient by Dr. Charles A. Mead, an orthopedist at the Naval Hosiptal clinic. Dr. Mead noted certain deformities in Mrs. Madrigan's feet, recommended surgical operations on her feet, and directed Mrs. Madrigan to return to the clinic for a final decision on the proposed foot surgery (App. 2a). Because Dr. Mead thought Mrs. Madrigan might be admitted to the hospital for surgery, "a routine pre-operative chest x-ray" of Mrs. Madrigan was taken on October 24, 1951 (App. 2a).

On October 29, 1951, Mrs. Madrigan was seen, again as an out-patient, by Dr. Mead and Dr. Cruise, the

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[2] 28 U.S.C. 1346(b); 28 U.S.C. 2671 *et seq.*

[3] A companion suit by Commander Madrigan as guardian *ad litem* for the minor children, Robert E. and Patricia Ann Madrigan, was consolidated for all purposes by the District Court. A single judgment (App. 8a-9a) disposing of both suits was entered by the District Court.

Chief of Orthopedics at the hospital. At this consultation it was decided not to perform surgery at that time; that, instead, Mrs. Madrigan should try foot baths and massage for her feet and a change of shoes (App. 3a). Mrs. Madrigan was directed to return to the clinic in one month for a check on her progress (App. 3a). After the examination of October 29, Mrs. Madrigan never returned to the Naval Hospital at Oakland (App. 4a).

The chest x-ray of Mrs. Madrigan, taken on October 24, 1951, was read by Dr. Bulgrin, a radiologist, on November 8, 1951. The x-ray film and a copy of Dr. Bulgrin's report of his reading of the film, dated November 9, were placed in the x-ray film files of the hospital.[4] The original of Dr. Bulgrin's report was, on or about November 9, 1951, placed in the out-patient file or jacket maintained at the hospital for Mrs. Madrigan (App. 3a). As to the x-ray of 1951, the district court found as follows (App. 4a):

> 11. The signs and shadows in said x-ray film which were the basis of said report of said radiologist [Dr. Bulgrin] and his reading, were vague, faint and indefinite, and were questionable and inclusive as evidence of any disease.

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[4] Dr. Bulgrin's report reads in part as follows (App. 3a): "11-8-51 CHEST, PA—

On the left in the plane of the first two anterior inter-spaces and to a lesser extent in the apex there is fine spotting and semi-confluent infiltration which is not heavy. Its appearance suggests minimal fibrotic infiltration.

Elsewhere the lung fields show no infiltration and the heart and other structures are unremarkable.

IMPRESSION: Minimal fibrotic appearing infiltration left upper lung field. Acid fast re-infection etiology must be considered first. Activity by single film study is not likely, but serial films over a fairly prolonged period are necessary to evaluate activity from a radiographic standpoint."

It was not until after May 1955, following the diagnosis in Japan of her tubercular condition, that Mrs. Madrigan made any inquiry of the routine pre-operative chest x-ray of October 24, 1951 (App. 4a). With further reference to the 1951 x-ray, the court found (App. 6a) that "whatever * * * [Mrs.] Madrigan's chest or lung condition was in 1951, as reflected in said October 24, 1951 chest x-ray film, such condition was not related to * * * [Mrs.] Madrigan's far advanced, active, bilateral, pulmonary tuberculosis in Japan in May, 1955."

With respect to the operation of the Naval Hospital at Oakland, the court found that the hospital was "operated and maintained with that degree of skill and care and knowledge and prudence that is ordinarily possessed and reasonably exercised by professional men, members of the medical profession * * *" (App. 5a-6a). And with further reference to incidents which took place at the Naval Hospital in Oakland in 1951, the Court found that there was no causal connection between the disease and disabilities of Mrs. Madrigan in 1955 and the operation, routine, maintenance, activities, acts, or alleged omissions, of the hospital or its personnel (App. 6a). Finally, the court found that neither the disease, disability nor the damage sustained by Mrs. Madrigan was caused by or was the result of any negligence, carelessness, wrongful act or omission on the part of the Oakland Naval Hospital or employees (App.).

These findings were totally dispositive of the Madrigans' claims based, as they were, upon the 1951 x-ray and the operation and procedures of the Naval Hospital in 1951. Accordingly, the District Court concluded (App. 6a-7a) that there was no basis for im-

posing liability upon the United States and entered judgment for the United States (App. 8a-9a).[5]

ARGUMENT

The District Court Correctly Held That in the Circumstances of This Case There Is No Legal Basis for Imposing Tort Liability Upon the United States

These suits arise under the Federal Tort Claims Act (28 U.S.C. 1346(b); 2671 *et seq.*) and, in accordance with the terms of that Act, the liability, *vel non,* of the United States is controlled and measured by the law of California where, in 1951, the alleged negligence or malpractice of naval medical personnel occurred. 28 U.S.C. 1346(b); 2674. This legal principle was not an issue in the trial court nor is it an issue on this appeal;[6] similarly, there was no issue below, nor is there in this Court, over the burden imposed by California law upon one who asserts a malpractice claim against a physican or surgeon.

The California law in this area is in accord with the general rule[7] and has been frequently stated and applied: See, *e.g., Lawless* v. *Calaway,* 24 Cal. 2d 81, 147 P. 2d 604; *Costa* v. *Regents of University of California,* 116 Cal. App. 2d 445, 254 P. 2d 85; *Ries* v. *Reinard,* 47 Cal. App. 2d 116, 117 P. 2d 386; *Sim* v.

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[5] This disposition of the case rendered it unnecessary for the District Court to consider or pass upon the Government's affirmative defense based upon the two year statutory limitation on tort actions in 28 U.S.C. 2401(b). In view of the plain correctness of the decision below on the merits we do not consider it necessary to press the point in this Court.

[6] See, Appellants' Br. p. 13. *Eastern Air Lines* v. *United States,* 221 F. 2d 62 (C.A.D.C.), affirmed *sub nom. United States* v. *Union Trust Co.,* 350 U.S. 907.

[7] 41 Am. Jur., *Physicians and Surgeons,* § 82; 70 C.J.S., *Physicians and Surgeons,* § 41.

Weeks, 7 Cal. App. 2d 28, 45 P. 2d 350; *Bruce* v. *United States,* 167 F. Supp. 579 (D. Cal.).

Stated generally, California requires that to sustain a suit for malpractice it must be proved that the injury, disease or disability was occasioned by the failure of medical personnel to exercise the degree of learning, diligence and skill ordinarily possessed by physicians and surgeons of good standing practicing in the same locality.

The judgment of the court below represents a proper application of this legal standard to the facts as determined by the trial judge. It is for this reason that the appeal in this case is necessarily directed to the factual findings of the trial court. And in view of the exclusively factual issues presented by the appeal it shall be our primary purpose to demonstrate that the critical findings of fact which underlay the judgment below are not "clearly erroneous" but are firmly grounded upon substantial evidence. For this reason, the findings should not be overturned and the judgment below, based on the findings, should be affirmed. Rule 52(a), Fed. Rules Civ. Proc.; *Pool* v. *Commissioner of Internal Revenue,* 251 F. 2d 233, 247 (C.A. 9); *Hennessey* v. *United States,* 242 F. 2d 381, 382 (C.A. 9).

A. The District Court Correctly Found That Mrs. Madrigan's Lung Condition in 1951 Was Not Related To Her Tubercular Condition in 1955.

With respect to the October 24, 1951 x-ray of Mrs. Madrigan's chest, the District Court found (App. 4a) that the signs and shadows in that x-ray film "were vague, faint and indefinite, and were questionable and inconclusive as evidence of any disease." In the teeth of this finding, appellants, in this Court, proceed on

the premise that, at this early date, Mrs. Madrigan was afflicted with tuberculosis and that her subsequent advanced tubercular condition in 1955 was proximately related to the alleged negligence of Government personnel in 1951 (Appellants' brief, pp. 17-19). We postpone for now our showing that the court's finding with respect to the controversial 1951 x-ray and the absence of negligence in 1951 are amply supported by substantial evidence and pass to what we consider an equally fundamantal infirmity in appellants' case. For the district court found, as additional facts (App. p. 6a) that whatever Mrs. Madrigan's chest or lung condition was in 1951, as reflected in the October 24, 1951 chest x-ray film, her condition was *not related* to Mrs. Madrigan's far-advanced, active, bilateral, pulmonary tuberculosis diagnosed in Japan in May 1955 and that there was no causal relation between appellants' illness and the events which transpired in 1951 (App. 6a). These findings, we now show, are clearly correct and are sufficient to dispose of appellants' claims.

As is common in suits based upon medical malpractice, questions of fact almost inevitably must be resolved on the basis of expert medical testimony. See, *e.g., Hennessey* v. *United States,* 242 F. 2d 381 (C.A. 9). This case is no exception. Both appellants and the United States presented to the trial court, members of the medical profession distinguished in the field of chest diseases. The principal witness for the Government was Dr. Horton Corwin Hinshaw. Following his graduation from the University of Pennsylvania Medical School in 1933, Dr. Hinshaw went directly to the Mayo Clinic where he remained until 1949, when he came to San Francisco where he pres-

ently resides. For fifteen years Dr. Hinshaw specialized in the field of chest diseases; he has taught in the School of Medicine, Stanford University, where he is Clinical Professor of Medicine and head of the Division of Chest Diseases in that University (Tr. 414-415). Dr. Hinshaw has published numerous papers in medical journals, co-authored a book on streptomycin in 1949,[8] and co-authored a textbook on diseases of the chest in 1956. Dr. Hinshaw has been the president of the American Trudeaux Society which is the medical section of the National Tuberculosis Association. He is a member of the Board of Directors of the National Tuberculosis Association of the State Tuberculosis Association and the San Francisco County Association (Tr. 416). He has served as a consultant to the Surgeon General of the Public Health Service for five years and at present is a consultant in tuberculosis to the State of California, Department of Public Health; he is also a consultant to Letterman Army Hospital, to the Naval Hospital at Oakland, California, and to the Parks Air Force Base Hospital (Tr. 416).

Dr. Hinshaw's qualifications as a medical expert in the field of tuberculosis are unquestionable. At the request of the United States Dr. Hinshaw reviewed the medical history of Mrs. Madrigan, conducted a physical examination of her, including an x-ray of her chest, and reviewed the medical records of previous examinations and x-rays in order to form an opinion as to the factors that may have been involved in the production of her illness diagnosed as tuberculosis in

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[8] Dr. Hinshaw and his associates were the first to use streptomycin in the treatment of tuberculosis, both in experimental animals and in human beings (Tr. 415-416).

1955. The medical history of Mrs. Madrigan, as obtained from medical records and from Mrs. Madrigan, as related by Dr. Hinshaw, is a follows:[9]

The records of the United States Naval Hospital, Portsmouth, Virginia, for 1948 and 1950, relate primarily to Mrs. Madrigan's two pregnancies and deliveries. In addition to the usual entries concerning her pregancies and deliveries, there is mention of Mrs. Madrigan having complained of sinking attacks and of fainting. On one occasion there was a mention of pleurisy "which may or may not be related to her current illness." There was no evidence of any x-ray of her chest having been made prior to 1948 although x-ray films were available in connection with her pregnancy in 1948 and 1950. "There was one film dated August 30, 1948, which, in my opinion, was free of evidence of disease" (Tr. p. 418). A second film, dated March 10, 1950 "was reported negative, and may or may not be negative. There is a suggestion of some possible early disease. It could represent early tuberculosis at that time, although I doubt if I would have reported it as such if I had been inspecting that film at that time. Only in retrospect has that possibility occurred to me * * *" (Tr. p. 419). Medical records with respect to Mrs. Madrigan for 1948 reveal, additionally, that following her first pregnancy she left the hospital of her own will and "with the knowledge that her physicians considered it unwise for her to leave at that time" (Tr. p. 420).

Upon her arrival in California in 1951 Mrs. Madrigan was seen on several occasions in August and September at the out-patient clinic at the Alameda

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[9] See also the testimony of Dr. Shipman, presented as a witness for the United States (Tr. 376-411).

Naval Air Station. The records there reveal that her first complaint, on August 31, 1951, was of dizzy spells and of fainting (Tr. p. 418). At that time an effort was made to find out why she was feeling dizzy and faint. "It was mentioned that she had had a miscarriage some three months previously and had been feeling weak since that date. It was suspected that she might be anemic, [but] her blood count was approximately normal. She had 75 percent hemoglobin. We ordinarily consider 80 percent to be normal for women. So is was slightly below normal" (Tr. pp. 420-421). On September 4, 1951, Mrs. Madrigan was given a prescription for iron and vitamins and was advised to return in one month.

On October 12, 1951, Mrs. Madrigan was referred to the orthopedic department of the Naval Hospital at Oakland, California. The entry on that date indicates that she was suffering from very painful feet. The orthopedic consultant, who examined Mrs. Madrigan, Dr. Mead, thought that the bunion deformity (hallux valgus) which he found was sufficient to justify an operation to relieve her painful condition. There is a further notation, on October 12, 1951, that Mrs. Madrigan wished to have both feet operated on at the same time and signed a form giving permission to have the operation performed. Dr. Mead, however, wished to have the Chief of Orthopedics, Dr. Cruise, see Mrs. Madrigan and help determine what type of operation, if any, should be done (Tr. p. 421). On October 24 while awaiting the consultation with the Chief of Orthopedics, Dr. Mead sent Mrs. Madrigan to have x-ray examinations made of her feet and a "routine pre-operative chest" x-ray examination.

Mrs. Madrigan was seen by the Chief of Orthopedics

on October 29, 1951, whereupon it was decided not to operate at that time. She was, instead, instructed, first, "to treat her feet with contrast baths twice a day, with foot massage twice a day. She was given advice with respect to the type of shoes she should wear, *and was instructed to return in one month, for a check on her progress*" (Tr. pp. 423-424) (Emphasis added). Contrary to her doctor's instruction to return in one month, Dr. Hinshaw "found no record that Mrs. Madrigan did return in one month, or, indeed, at any other time, to Oakland Naval Hospital until 1955, when she came back from Japan" (Tr. p. 424). Mrs. Madrigan did, however, tell Dr. Hinshaw that she attended the out-patient clinic at Alameda in December, 1951 when she had symptoms of sinusitis and an x-ray of her sinuses at that time disclosed evidence of sinusitus. She was given a series of penicillin injections and apparently there was no other indication of disorder along that line (Tr. p. 424).

A clinical notation made on May 12, 1952, discloses that Mrs. Madrigan was given a prescription for a drug known as Texamyl. This drug is frequently given to people who are depressed and emotionally disturbed, and "sometimes is given in connection with the treatment of alcoholism, although there is no record that she had any problem with alcoholism at that time" (Tr. p. 424).

Continuing with his narration of Mrs. Madrigan's medical history, Dr. Hinshaw found the next entry under date of April 16, 1953, where the statement appears, "Possible anemia and nervousness." A blood count was done and the results were within normal limits (Tr. p. 426). With particular reference to the period commencing in 1948 through April 16, 1953

Dr. Hinshaw could find no entry in Mrs. Madrigan's medical record "which would lead me to suspect active tuberculosis, and evidently the attending physicians, who must have had a much better insight into her problems at the time, did not order any x-rays or other examinations, which leads me to believe that they also did not regard any of her symptoms as indicative of tuberculosis" (Tr. p. 426).

Subsequent to April 16, 1953, Mrs. Madrigan was given a physical examination prior to her embarkation for Japan. There is no indication as to what this examination consisted of but it was evidently satisfactory inasmuch as the medical entry "is simply an O.K., a date, and the initials or signature" (Tr. p. 427). The next entry in Mrs. Madrigan's clinical record is of her admission to the United States hospital in Japan on March 16, 1954, where she remained until March 19, 1954. The record with respect to this hospitalization reveals that Mrs. Madrigan, prior to her admission, "had been drinking, consuming one-fifth gallon of whisky per day for several days previously; that she had been complaining of severe nervousness for the previous two years; and that her drinking had been because of her nervousness. She also had been vomiting excessively; * * * had been emotionally disturbed;" (Tr. p. 428). Mrs. Madrigan was treated with vitamins, a diet and when she left the hospital on March 19 was very much improved. On October 14, 1954, Mrs. Madrigan was again admitted to the hospital in Japan where she remained until October 20. The hospital record disclosed "that she and her husband had had frequent arguments over many years, and that during the one year that they had been overseas they had been constantly fighting between themselves

because of the patient's excessive drinking and because of her husband's alleged infidelity. The statement was also made that she had had frequent temper outbursts, a loud and obnoxious behavior, which had come to the attention of neighbors and administrative officials at the camp at Yokahama. Prior to entering the hospital [Mrs. Madrigan] had become very nauseated, and apparently she had eaten nothing for several days. The examiners reported her to be very much disturbed emotionally; that at the time [October 24, 1954] she had been hostile and antagonistic, and had uncontrolled temper outbursts" (Tr. pp. 428-429).

On November 10, 1954, Mrs. Madrigan was apparently seen as an out-patient at the hospital where the diagnosis was simply: "Entered as emotional instability reaction" (Tr. p. 429).

Mrs. Madrigan was admitted to the U. S. Naval Hospital No. 3293 in Japan on May 13, 1955 "because of excessive drinking, nervousness, emotional instability, and cough. She had lost weight. And again the entry is made that she had been consuming approximately one-fifth gallon of whisky daily. When she was examined at that time, and for the first time that I could find in her record, there were abnormal physical signs in her chest. * * * The physical examination of her chest suggested to the examiner that she might have an asthmatic condition, but X-ray examinations were ordered, and these showed a very extensive, what I would regard as an acute type of pulmonary tuberculosis" (Tr. pp. 429-430). At that time her sputum was found to contain tubercule bacilli, and Mrs. Madrigan's condition was recognized as a very acute, serious, pulmonary infection with tuberculosis" (Tr. p. 430).

Having reviewed Mrs. Madrigan's x-rays in May 1955, Dr. Hinshaw related that he agreed, with the radiologist who interpreted those x-rays, that Mrs. Madrigan at that time "had very extensive tuberculosis of an acute inflammatory type which involved nearly all portions of both lungs. The shadows were most dense at both apices, and there were probably multiple small cavities on both sides" (Tr. p. 431). The 1955 x-rays indicated "inflammation which involved essentially all portion of both lungs, most intense in the upper portion of each lung" (Tr. p. 440) and while "one could not say with absolute assurance that this was tuberculosis by looking at the x-ray, although [it was] surely very strongly suspicious of tuberculosis * * *" (Tr. p. 440). The signs and shadows present in the 1955 x-rays were described by Dr. Hinshaw "as acute. *By 'acute,' I mean of recent origin. One cannot always read the past in an x-ray film, but when one sees this type of shadow he is justified in saying that this is a disease of recent origin. Most of what we saw certainly had not been there many months previously, and possibly not many weeks previously*" (Emphasis added) (Tr. 441).

Dr. Hinshaw was thus of the opinion that on the basis of the x-ray evidence of Mrs. Madrigan's tubercular condition in 1955 her lung condition was of "recent origin * * * and had not been there many months previously and possibly not many weeks previously" (Tr. 441). Dr. Hinshaw found confirmation of this opinion in subsequent x-ray films taken of Mrs. Madrigan after her removal from Japan to Fitzsimmons Army Hospital, Denver, Colorado. Within several weeks following Mrs. Madrigan's diagnosis in May 1955 "there was a marked diminution in the

amount of imflammation". This factor is significant, in the words of Dr. Hinshaw, "because we know that inflammation of recent origin also disappears much more rapidly and much more completely, so that at present [December 27, 1957, Mrs. Madrigan shows] essentially no inflammatory reaction and remarkably little scar tissue. If her disease had been present for a long time prior to the institution of treatment I would have anticipated seeing a great deal of scar tissue in the lungs at this time, whereas there is very little" (Tr. p. 441).

Dr. Hinshaw's opinion that Mrs. Madrigan's condition in 1955 was of "recent origin" was further confirmed by the "tuberculin inflammation of [Mrs. Madrigan's bronchia]" in May, 1955. (Tr. p. 441). In the words of Dr. Hinshaw tuberculin inflammation of the bronchia "is also indicative of a very acute disease. That is, when tuberculous ulceration of the bronchia—that is, ulcerative changes in the membrane which lines the air-conducting tubes—when that occurs there is often a rather rapid, almost explosive-like spread of the disease to many parts of the lung * * *" (Tr. p. 442). Still further confirmation of the "recent origin" of Mrs. Madrigan's tubercular condition in 1955 is found in the fact, relied upon by Dr. Hinshaw, that skin tests on Mrs. Madrigan's two children were performed "a few months" prior to May 1955 (Tr. p. 446). This fact is significant "because a tuberculous mother very readily transmits the disease to her children by the very nature of their intimate and oft repeated contact. It's quite unusual indeed to find a lady with tuberculosis whose children are tuberculin negative. * * * If she had had tuberculosis in an open form since 1951, I do not believe the children would

have had negative skin tests a few months prior to May 1955" (Tr. 446).

Based upon the careful analysis and opinion of Dr. Hinshaw, a distinguished specialist in the field of chest diseases, there can we submit, be no serious question that the finding of the district court that Mrs. Madrigan's tubercular condition in 1955, was not related to her lung condition in 1951 whatever it may have been. And there is more to support this finding of the District Court. Again we draw upon the testimony of Dr. Hinshaw and quote from his relevant and instructive opinion as to the probable causes of the acute tubercular condition of Mrs. Madrigan in 1955 (Tr. pp .450-452):

> Well, as with every case of tuberculosis, there first must be the factor of infection. Where she acquired her infection and when, we have no idea. It is true that infection is much more readily acquired in the Orient than it is in this country, and it is possible she first acquired it over there. But I think it would be fruitless to attempt to guess where she first acquired her tuberculosis. We know the infection is acquired by essentially everyone who lives in the Orient for any length of time. It's acquired, was acquired, essentially by everyone in this country, perhaps, say, one or two generations ago. At present it is not nearly so prevalent. But the infection itself is not ordinarily manifested by disease; commonly tuberculosis enters the system, heals in the normal course of events partially but not totally, and then is reactivated at some later date as a result of environmental influences. That is why tuberculosis is so spoken of as a "social disease" or a "social disorder," and is why tuberculosis is so common in those countries where nutrition is poor and where

people work hard and don't get adequate rest and so on.

That is why tuberculosis is rare in this country, why it is common in the Orient, why it is common in Russia and other countries. When tuberculosis exists, we nearly always try to find out if we can what are the facts, why did this person become ill when other ones who became infected were not rendered ill and such things as child-bearing frequently enter into it with women—loss of sleep, overwork, malnutrition are very commonly an important factor, among underprivileged people, and those who have had bad nutritional habits. And one of the very common causes, one of the very common factors to which we attribute the breakdown of tuberculosis, is alcoholism.

I should say that in San Franciso Hospital, which of course does deal with a different class of society from that of Mrs. Madrigan, but nevertheless in San Francisco Hospital I should say that in the service that I have supervised there for the past seven or eight years, I should say 50% of our patients, or perhaps more, have an alcoholic history and have a connection between alcoholic excesses and specific, breakdown of tuberculosis prior to admission.

When I was consulting medical director to another institution, Weimar Chest Center, where we have five or six hundred admissions a year,—again these are patients of the indigent class; nevertheless, alcoholism enters in very frequently as a cause of acute flareup of pulmonary tuberculosis.

It is my opinion that in Mrs. Madrigan's case, she might well have remained well, she might well have escaped what she has gone through, if she had been of more temperate habit. I think it's not alone the alcohol per se, it is also the starvation and malnutrition that such people impose

upon themselves. Many have the feeling that the emotional factors, in themselves, quite independent of any toxic material or malnutrition, may affect the progress of tuberculosis unfavorably. The mechanism of that is perhaps along the line of the cortisone drugs, which are definitely more likely to be in quantity in the body following emotional crises. And very often pulmonary tuberculosis seems to be the result of the emotional crises' even when alcoholism and malnutrition do not enter.

So I would sum it up by saying that I think her intemperate habits and her emotional problems, her misfortunes, were the most important causes of her tuberculosis.

By way of summation then, the evidentiary facts supporting the District Court's finding that Mrs. Madrigan's tubercular condition in 1955 was of "recent origin" and therefore not related to her lung condition in 1951, whatever it may have been, as reflected in the 1951 x-ray, as follows: (1) the medical history of Mrs. Madrigan prior to 1955 does not reflect symptoms which would lead one to suspect that she had tuberculosis; (2) Mrs. Madrigan's diagnosis of tuberculosis took place in the Orient where tuberculosis is common and infection is acquired by essentially everyone who lives in the Orient for any length of time (Tr. 450); (3) Mrs. Madrigan's excessive consumption of alcohol and the concomitant of alcoholism, malnutrition, were evident while she was in Japan and immediately preceding her diagnosis of tuberculosis; (4) Mrs. Madrigan, immediately prior to her diagnosis, had been beset with emotional problems and domestic difficulties which were symptomatic of either or both her alcoholism and her husband's asserted in-

fidelity; (5) Mrs. Madrigan's tuberculosis was "acute" when diagnosed in May 1955 and, following treatment the inflammation disappeared rapidly and left very little scar tissue; and (6) the skin tests of Mrs. Madrigan's children, a few months prior to May 1955, were tuberculosis "negative" although a "tuberculin mother readily transmits the disease to her children by the very nature of their intimate and oft repeated contact" (Tr. 446).

B. The District Court's Finding That Government Personnel Were Not Negligent in 1951 Is Clearly Correct.

1. Appellants' claims turn upon events which transpired at the out-patient clinic of the Naval hospital in Oakland, California, in 1951. With respect to these events and to the action of medical personnel, the district Court found (App. 5a-6a):

> [That] there was no negligence, or carelessness, and no wrongful act, or omission on the part of defendant the United States of America or its employees, * * * and at all times pertinent to the issues herein said United States Naval Hospital at Oakland, California, was operated and maintained with that degree of skill and care and knowledge and prudence that is ordinarily possessed and reasonably exercised by professional men, members of the medical profession, under all the circumstances of this case.

By way of attack upon this finding, appellants point to the controversial x-ray of Mrs. Madrigan's chest taken in 1951 and argue that by any reasonable standard of good medical practice, that x-ray should have been in her jacket when she arrived for surgery on October 29, 1951 (App. Brief, p. 21). This argument is based on the supposition that Mrs. Madri-

gan, in 1951, was, at that time, afflicted with tuberculosis, either active or inactive, and that the 1951 x-ray is conclusive evidence of this asserted fact. With respect to the x-ray the District Court found, however, that (App. 4a) "the signs and shadows in said x-ray film which were the basis of said report of said radiologist in his said reading, were vague, faint and indefinite, and were questionable and inconclusive evidence of any disease."

With wisdom born largely of hindsight there was opinion testimony by competent medical personnel that the 1951 x-ray was indicative of active or incipient tuberculosis and that Mrs. Madrigan's condition in 1955 was the culmination of a progressive disease. Such testimony does not impair the finding of the trial court, however, much less permit it to be set aside, for as we have shown there is opinion testimony that her condition in 1955 was of recent origin. Additionally, it is a fact that is not subject to dispute that no one will ever know with any degree of certainty what the true state of Mrs. Madrigan's lung condition was in 1951, nor can there be any dispute that it is virtually impossible to diagnose the disease of tuberculosis on the basis of a single x-ray (Tr. 389). In this regard, we point out that even in 1955 when Mrs. Madrigan's tuberculous condition was diagnosed, the diagnosis could not be made on the basis of her x-rays alone but was conclusively established only after a sputum test revealed the presence of tubercule bacilli (Tr. p. 430).

Neither is the finding of the trial court impeached because the radiologist who read the 1951 x-ray was of the opinion that the signs and shadows might be indicative of "acid fast re-infection etiology"—in

medical parlance, tuberculosis—which must be "considered first" (App. 3a). Nor to support the finding is it necessary to impeach the radiologist's report. On the contrary, all medical experts in the court below were of the view that the 1951 x-ray was competently read and reported. Thus, Dr. Hinshaw testified that in the x-rays "there are shadows, again very faint, and some detectable, strand-like shadows more indicative of a scarring process than that of an inflammatory process" (Tr. 538). "What we are seeing there [in the x-ray], * * * is the result of infection rather than the inflammatory reaction itself. *A scarring process refers to the result of an infection rather than the infection itself,* and it may well have been healed and it may well have not been. There is no way of knowing. * * * It could have been active or it could have been inactive" (Tr. pp. 538-539).

Even had there been an active infection in 1951, "in the normal course of events * * * if you had 100 patients, let us say, with shadows comparable to this, that of those 100 maybe 95—a large proportion of them—would never have come to any recognizable disease. We see scars and even calcified areas of healed tuberculosis in the chest x-rays of thousands of people who have never known themselves to be ill, who must have had this much or more disease at some remote period. That is why I emphasized * * * the environmental factor. What were the factors which caused her infection to become active and symptomatic and devastating—appearing as it did in 1955 * * * The normal course of events would be for it [the pathology]to heal if she were living under good conditions" (Tr. pp. 538-539).

The predicate for appellants' claims—that Mrs. Madrigan had active or incipient tuberculosis in 1951—is necessarily based upon conjecture. Not only is it questionable that the "signs and shadows" disclosed by the 1951 x-ray were present because of a tuberculosis infection but even if she were tubercular at that time, it is questionable whether the evidence was of active tuberculosis or whether it was evidence of a prior infection that had subsequently healed. In short, the signs and shadows, as the District Court found, were questionable and inconclusive of any disease. And the speculative nature of these claims is the more apparent in the light of the fact that the signs and shadows present in the x-ray could as well be attributable to "some acute, transient, infection related to [Mrs. Madrigan's] sinusitus, for example. It is possible that it might have been some fungus infection, a coccidioidomycosis, which is common in parts of California, * * * [produces] shadows, [Tr. pp. 437-438] * * * and is a frequent cause of mis-diagnosis" (Tr. p. 439). Moreover, "it is not infrequent that patients develop shadows of this sort presumably due to viral infections * * * which will often disappear without ever knowing what they were" (Tr. pp. 439-444).

And the possibility cannot be "excluded" that the signs and shadows in the 1951 x-ray were the result of artifacts, meaning that they were produced by some "artificial, external condition" (Tr. p. 548). Dr. Hinshaw has seen "shadows before precisely like those [in the 1951 x-ray] cast by braids of hair, * * * parts of clothing—a silk handkerchief * * * has created a shadow that was all for the world like a serious-looking area of disease" (Tr. p. 549). It is not of

course essential that the signs and shadows in the 1951 x-ray were attributable to a factor other than tuberculosis; all that need be shown is, as we have done, that the record is replete with substantial evidence supporting the District Court's finding that the signs and shadows in the x-ray were "questionable and inconclusive as evidence of any disease" (App. 4a).

2. In finding that medical personnel at the Naval Hospital in Oakland were not negligent in 1951, the District Court assayed their conduct in the light of the degree of learning, diligence and skill ordinarily possessed by physicians and surgeons of good standing practicing in the San Francisco area. *Lawless* v. *Calaway,* 24 Cal. 2d 81, 86, 147 P. 2d 604. In weighing the correctness of the finding that Government personnel were not negligent it must be remembered that the 1951 x-ray of Mrs. Madrigan's chest was not taken because she was complaining of a respiratory ailment. Rather, her complaint in 1951, when she presented herself to the out-patient clinic, was of a foot condition, hallux valgus—bunion growths which were so extensive that the examining orthopedist, Dr. Mead, recommended that surgery be performed. The x-ray which he ordered was a "pre-operative chest x-ray", a routine hospital procedure. Surgery, however, was never performed upon Mrs. Madrigan because the Chief of Orthopedics, Dr. Cruise, on examining Mrs. Madrigan, was of the view that her condition could be corrected by less drastic measures. There was, therefore, no necessity and no occasion for the "routine pre-operative chest x-ray" ever to come to the attention of Dr. Mead or his superior, Dr. Cruise; and, insofar as appears, the x-ray was not, in fact, seen by any doctor other than the radiologist who read the x-ray until

appellants dug the x-ray out of the hospital files some four years later.

In these circumstances, there is no basis whatever for charging either Dr. Mead or Dr. Cruise with malpractice because follow up measures with respect to the x-ray were not taken; and no criticism can validly be directed at Dr. Bulgrin, the radiologist, because his only job and his only responsibility was to read the x-ray and it is agreed that this job he did with complete competence (App. 14a-15a).

Neither can it be said that the operating routine at the Naval hospital provides a basis upon which to sustain these claims. Mrs. Madrigan was instructed by her physician, on October 29, 1951, to return to the out-patient clinic in one month in order to ascertain whether the corrective measures, short of surgery, were remedying the condition of her feet. The x-ray of Mrs. Madrigan's chest was read on November 8 and Dr. Bulgrin's report was typed on November 9, 1951. The x-ray and the report, in due course, found their way to the jacket maintained for Mrs. Madrigan at the clinic. Had she complied with her physician's instruction and returned to the clinic within a month or even later, the radiologist's report on the chest x-ray would, presumably, have then come to the attention of a physician whereupon the follow-up measures which everyone agrees were warranted by the x-ray, would, presumably, have been taken (Tr. 399).

The manner in which the out-patient clinic was conducted, with particular reference to the x-ray procedures, in no way departs from the procedures followed in clinics of comparable institutions in the San Francisco area. Dr. Hinshaw is chief of the chest out-patient clinic at Stanford Hospital and is familiar

with the chest clinic at San Francisco Hospital and has worked in some other institutions. Dr. Hinshaw was asked by the court (Tr. p. 459), "What is the ordinary and usual business and professional practice of hospitals and hospital personnel and doctors, experts in your field, such as you are, and with out-patient and in-patients and so on with respect to those matters." Dr. Hinshaw answered as follows (Tr. 459):

> My knowledge of Oak Knoll Naval Hospital is based upon the fact that I go over on the first and third Wednesdays of each month and consult with the physicians there concerning special problems, usually perplexing problems relating to lung disease and very often based upon x-ray findings. These are ordinarily, although not invariably, in-patients rather than out-patients. I have observed, though, that the personnel in the hospital—and I am reasonably sure in the out-patient department also—changes frequently, and that everything is entered in the record, so that a continuation of responsibility from one man to another is achieved by reference to the record. And one who does not have the record in hand is almost hopelessly ignorant of that particular patient. You might say the same thing applies to out-patient departments elsewhere, such as Stanford Hospital. I will see the patient one day, perhaps someone may see him next time, and each time we try to enter it in the record. And if the patient does not return, the record is not recalled and there is no way of determining what may have happened during the patient's absence. If the patient is directed to return, it is anticipated of course that when that patient does return, everything will be brought up-to-date, brought together, and the patient will be informed of what needs to be done. If the patient fails to return, then those

things may well be lost through observation, like it was in this woman's case.

It is my opinion that her failure to be informed, assuming that her memory is correct and she was not informed, was due to the fact that she never returned to the place where that information was placed. Her subsequent visits were to a different institution (Emphasis added).[10]

There can, we submit, be no serious question that the findings of fact of the District Court in this case are supported by substantial evidence. We have, moreover, through the District Court's opinion, the benefit of some of the considerations which he took into account in making his findings. Thus, his opinion reveals with marked clarity that not the least factor underlying his findings was the demeanor and stature of the professional men who were before the court. Thus, with respect to Dr. Hinshaw, the court said: (App. 10a):

"[he] had the bearing and demeanor of a scientist and in what he said, he expressed himself with careful attention to detail and the thoughtful attention to his phrases, to their meaning and extent. Now, without casting any uncomplimentary suggestion upon Dr. Bulgrin, I suggest to you that the testimony of Dr. Hinshaw in my judgment is the more credible."

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[10] A serviceman's dependent is not, of course, subject to military discipline and there is no more an obligation upon medical personnel of the services to pursue a patient than there is upon a private physician or surgeon. *Urrutia* v. *Patino, et al.*, 297 S.W. 2d 512, 516 (Civ. App. Tex.); *Local Union 6068 of United Mine Workers* v. *Bizzell,* 257 S.W. 2d 527 (Ky.); and *Miles* v. *Harris,* 194 S.W. 839, 844 (Civ. App. Tex.).

With reference to Dr. Bulgrin the court said (App. 9a-10a):

> Now, to start out with, I am going to pay a little attention to Dr. Bulgrin. And that statement of his that the chances were overwhelming that Mrs. Madrigan had tuberculosis in the upper left lobe of that lung on October 24, 1951.
>
> Now, one of the jobs of the trial judge is to pass upon the credibility of the witnesses and what they say. And I suggest to you that at the time Dr. Bulgrin said what he did about "overwhelming," I was sitting here with my eye on him, watching him. And Dr. Bulgrin relaxed, slumped down in his chair; it was the tale end of something he had been talking about, his attitude and manner of speech were such, and the character of his statement was such, that it seemed to me that that was a rather careless thing for a well-trained, experienced doctor to say. * * *

And the court observed that (App. 18a-19a):

> "* * * it is interesting to observe here that it is the younger ones, the least experienced, and those who haven't yet developed a very high degree of care in their observations and statements, who go the farthest in this record. Hinshaw and Shipman seem to me to come very close to stating just about all one can state concerning this evidence. I prefer to take the view that the credibility of Dr. Hinshaw's testimony here is to be preferred to the credibility of Kruisheer, the credibility of Bulgrin and the credibility of Dr. Wilson.
>
> "Dr. Wilson is a splendid man, but he is a young man. He has a wonderfully fine educational background and a good deal of experience, but I was of the opinion and am now that Dr. Wilson made of himself something of an advocate in this case,

and I don't suggest anything uncomplimentary to him or to counsel in that connection. He was just very enthusiastic about those films of his. * * *"

As this Court pointed out in *Pool* v. *Commissioner of Internal Revenue,* 251 F. 2d 233, 247, "The trier of fact may disregard uncontradicted testimony, if it is improbable. What is more important, he may make his own inferences from the demeanor of the witnesses' which is 'always assumed to be in evidence'."[11] In the circumstances of this case, turning as it does upon expert medical testimony, in some respects on conflicting testimony, particular deference is to be accorded the trier of fact. For this additional reason the findings should not be disturbed.

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[11] "Wigmore on Evidence, 3rd ed., 1940, Vol. III, § 946, p. 498. The late Judge Jerome Frank of the Court of Appeals for the Second Circuit has written what has become almost a classic comment on the significance of the demeanor of an orally-testifying witness as expressed in the brief statement quoted in the text from Wigmore:

> 'It is 'wordless language.' The liar's story may seem uncontradicted to one who merely reads it, yet it may be 'contradicted' in the trial court by his manner, his intonations, his grimaces, his gestures, and the like—all matters which 'cold print does not preserve' and which constitute 'lost evidence' so far as an upper court is concerned. For such a court, it has been said, even if it were called a 'rehearing court,' is not a 'reseeing court.' Only were we to have 'talking movies' of trials could it be otherwise. A 'stenographic transcript correct in every detail fails to reproduce tones of voice and hesitations of speech that often make a sentence mean the reverse of what the words signify. The best and most accurate record is like a dehydrated peach; it has neither the substance nor the flavor of the fruit before it was dried'. It resembles a pressed flower. The witness' demeanor, not apparent in the record, may alone have 'impeached' him.' (*Broadcast Music, Inc.* v. *Havana Madrid Restaurant Corp.,* 2 Cir., 1949, 175 F. 2d 77, 80.)" 251 F. 2d at 247-248, No. 28.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment in the District Court should be affirmed.

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Robert H. Schnacke,
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APPENDIX

APPENDIX

[Captions omitted]

Findings of Fact and Conclusions of Law

The above-entitled actions came on duly and regularly for consolidated hearing and trial on Monday, January 20, 1958, before the above-entitled court, upon the complaints of plaintiffs and the answer and amended answer of defendant the United States of America, the Honorable Willis W. Ritter presiding without jury. Plaintiffs Johnnie Elmease Madrigan and Fred J. Madrigan appeared in person, plaintiff Fred J. Madrigan appeared as guardian ad litem of plaintiffs Robert Edward Madrigan and Patricia Ann Madrigan, and all the plaintiffs appeared through their attorneys Melvin M. Belli, Esq., Lou Ashe, Esq. and Richard F. Gerry, Esq; and defendant the United States of America appeared by Lloyd H. Burke, United States Attorney for the Northern District of California, and James S. Higgins, Assistant United States Attorney. At the commencement of trial, upon motion of plaintiffs the court consolidated said actions for all purposes. Thereafter, evidence both oral and documentary was offered in evidence and received by the Court, and certain facts were stipulated to by the parties. The Court having heard all the testimony and all the evidence, said cause was thereafter argued by counsel, and it was thereafter duly and regularly submitted to the Court for its decision. Said cause was then considered by the Court and the Court thereupon made its order that judgment be entered herein, upon findings of fact and conclusions of law, in favor of defendant the United States of America,

The Court accordingly, being fully advised in the premises, now makes its findings of fact and states its conclusions of law as follows:

Findings of Fact

1. The complaints allege that these actions were commenced pursuant to, and that jurisdiction is founded

upon, the provisions of the Federal Tort Claims Act, 28 U.S.C. §§ 1346(b) et seq.

2. At all times mentioned in the complaints and herein, defendant the United States of America operated the United States Naval Hospital at Oakland, California, and United States Naval Hospital No. 3923 in Japan.

3. At all times mentioned in the complaints and herein, plaintiff Fred J. Madrigan was, and now is, a commissioned officer in the United States Navy, and his present rank is Commander.

4. On October 12, 1951, plaintiff Johnnie Elmease Madrigan, the dependent wife of plaintiff Fred J. Madrigan, went to the out-patient department of the United States Naval Hospital at Oakland, California, as an out-patient, complaining of very painful feet and fatigue.

5. On October 12, 1951, plaintiff Johnnie Elmease Madrigan was seen in the out-patient department of the United States Naval Hospital at Oakland, California by Dr. Robert F. Christoph, who diagnosed a condition of foot deformity known as hallux valgus and referred her to the orthopedic section of the out-patient clinic.

6. On October 24, 1951 plaintiff Johnnie Elmease Madrigan was seen as an out-patient by Dr. Charles A. Mead, an orthopedist at the United States Naval Hospital at Oakland, California, who noted certain deformities in her feet, recommended surgical operations on both feet, and directed plaintiff to return for the final decision upon the proposed foot surgery.

7. On October 24, 1951, at the United States Naval Hospital at Oakland, California, a routine pre-operative chest x-ray was taken by a technician of the chest of plaintiff Johnnie Elmease Madrigan because Dr. Mead, the orthopedist, thought Mrs. Madrigan might be admitted to the hospital for foot surgery.

8. On October 29, 1951 at the United States Naval Hospital at Oakland, California, plaintiff Johnnie Elmease Madrigan was seen again as an out-patient by Dr. Mead in consultation with the Chief of Orthopedics at said hospital, and it was dicided that plaintiff would have no surgery at that time, that she should try foot baths and massage for her feet and change her shoes, and plaintiff was directed to return to said hospital in one month for a check on her progress.

9. A report of a reading upon said chest x-ray dated November 9, 1951, and signed by the radiologist who read the x-ray and made the report, J. G. Bulgrin, CDR, MC, USN, reads in part as follows:

> "11-8-51 Chest, PA—
>
> On the left in the plane of the first two anterior interspaces and to a lesser extent in the apex there is fine spotting and semiconfluent infiltration which is not heavy. Its appearance suggests minimal fibrotic infiltration.
>
> Elsewhere the lung fields show no infiltration and the heart and other structures are unremarkable.
>
> Impressions Minimal fibrotic appearing infiltration left upper lung field. Acid fast re-infection etiology must be considered first. Activity by single film study is not likely, but serial films over a fairly prolonged period are necessary to evaluate activity from a radiographic standpoint."

10. Said chest x-ray film and a copy of said report of the said reading of said film were placed in the x-ray film files at the United States Naval Hospital at Oakland, California, and the original of said report was, on or about November 9, 1951 placed in the out-patient file or jacket maintained at said hospital for plaintiff Johnnie Elmease Madrigan.

11. The signs and shadows in said chest x-ray film which were the basis of said report of said radiologist of his said reading, were vague, faint and indefinite, and were questionable and inconclusive as evidence of any disease.

12. Plaintiff Johnnie Elmease Madrigan never returned to the United States Naval Hospital at Oakland, California, as directed on October 29, 1951.

13. Plaintiff Johnnie Elmease Madrigan made no inquiry with respect to the results of said chest x-ray and other studies until after May, 1955.

14. On May 13, 1955, plaintiff Johnnie Elmease Madrigan was admitted to United States Naval Hospital No. 3923 in Japan. Thereafter, a diagnosis was made that she had tuberculosis, pulmonary, bilateral, active, far-advanced.

15. On May 28, 1955, plaintiff Johnnie Elmease Madrigan was admitted to the United States Naval Hospital at Oakland, California. On June 13, 1955, plaintiff Johnnie Elmease Madrigan was admitted to Fitzsimons Army Hospital at Denver, Colorado. On November 2, 1955, plaintiff Johnnie Elmease Madrigan was admitted to the Parks Air Force Base Hospital in California.

16. On March 2, 1956, plaintiff Johnnie Elmease Madrigan completed her hospitalization at Parks Air Force Base Hospital in California, was discharged as an in-patient, and continued as an out-patient of said hospital.

17. Plaintiff Johnnie Elmease Madrigan is the mother of plaintiffs Robert Edward Madrigan and Patricia Ann Madrigan.

18. Sometime after May 13, 1955 there were indications of plaintiffs Robert Edward Madrigan and Patricia Ann Madrigan having been infected with tuberculosis.

19. On June 14, 1957, this court made an order appointing plaintiff Fred J. Madrigan guardian ad litem for plaintiffs Robert Edward Madrigan and Patricia Ann Madrigan.

20. Neither defendant the United States of America nor any employee of the Government was negligent or careless in the care, prescription, testing, treatment, diagnosis, examination, attention, or advice to plaintiff Johnnie Elmease Madrigan or in the operation and maintenance of said United States Naval Hospital at Oakland, California, or in any other respect.

21. No injury, disease, disability, or damage to plaintiffs, or any of them, was the result of any negligence or carelessness, or of any wrongful act or omission, in the manner in which defendant the United States of America and its employees operated and maintained said United States Naval Hospital at Oakland, California, or in any other respect.

22. None of the damages alleged or suffered, if any, by plaintiffs as a result of any injury, disease, or disability, were caused or contributed to by any negligence or carelessness, or any wrongful act or omission, on the part of defendant the United States of America or of its employees at the times and places and on the occasions alleged by plaintiffs in their complaints herein, or otherwise.

23. There was no negligence or carelessness, and no wrongful act or omission, on the part of defendant the United States of America or its employees, in any way connected with the matters alleged in the complaints herein and tried in this action, and at all times pertinent to the issues herein said United States Naval Hospital at Oakland, California was operated and maintained with that degree of skill and care and knowledge and prudence that is ordinarily possessed and reasonably exercised by professional men, mem-

bers of the medical profession, under all the circumstances of this case.

24. None of the incidents, matters, or things mentioned in the complaints or herein caused any injury, disease, disability, or damage to plaintiffs, or any of them.

25. None of the incidents, matters, or things mentioned in the complaints or herein or tried in this action concerning the operation, routine, maintenance, activities, acts, or alleged omissions, of said United States Naval Hospital at Oakland, California or of any Government employee caused any injury, disease, disability, or damage to plaintiffs, or any of them.

26. Whatever plaintiff Johnnie Elmease Madrigan's chest or lung condition was in 1951, as reflected in said October 24, 1951 chest x-ray film, such condition was not related to plaintiff Johnnie Elmease Madrigan's far advanced, active, bilateral, pulmonary tuberculosis in Japan in May, 1955.

Conclusions of Law

And as and for its conclusions of law the Court states as follows:

1. Neither defendant the United States of America nor any employee of the Government, was negligent or careless in the operation and maintenance of its United States Naval Hospital at Oakland, California at the times and places set forth in plaintiffs' complaints, or otherwise.

2. There was no act or omission on the part of defendant the United States of America or any of its employees imposing upon defendant the United States of America or any of its employees any liability or responsibility to plaintiffs, or any of them, on account of any injury, disease, disability, or damage to plain-

tiffs, or any of them, neither defendant the United States of America nor any of its employees caused or contributed to any injury, disease, disability, or damage to plaintiffs, or any of them, and there was no negligence on the part of defendant the United States of America or any of its employees that caused or contributed to any injury, disease, disability, or damage to plaintiffs, or any of them.

3. No act or omission of defendant the United States of America or any employee of the Government caused any injury, disease, disability, or damage to plaintiffs, or any of them.

4. Defendant the United States of America is not liable to plaintiffs, or any of them, or responsible to plaintiffs, or any of them, for any losses in respect of any injury, disease, disability, or damage to plaintiffs, or any of them, and no money or damages are due or owing by defendant the United States of America to plaintiffs, or any of them, on account of any injury, disease, disability, or damage to plaintiffs, or any of them.

5. Plaintiffs are not—and none of them is—entitled to recover anything from defendant the United States of America upon their said complaints or in this action.

6. Defendant the United States of America is entitled to judgment against plaintiffs, and each of them, in this action, together with its cost of suit incurred herein.

Let judgment be entered accordingly.

Done in Open Court this 17th day of February, 1958.

/s/ Willis W. Ritter
United States District Judge

[Captions omitted]

Judgment

The above-entitled actions came on duly and regularly for consolidated hearing and trial on Monday, January 20, 1958, before the above-entitled Court, upon the complaints of plaintiffs and the answer and amended answer of defendant the United States of America, the Honorable Willis W. Ritter presiding without jury, and plaintiffs Johnnie Elmease Madrigan and Fred J. Madrigan appearing in person, plaintiff Fred J. Madrigan appearing as guardian ad litem of plaintiffs Robert Edward Madrigan and Patricia Ann Madrigan, and all the plaintiffs appearing through their attorneys Melvin M. Belli, Esq., Lou Ashe, Esq., and Richard F. Gerry, Esq.; and defendant the United States of America appearing by Lloyd H. Burke, United States Attorney for the Northern District of California, and James S. Higgins, Assistant United States Attorney; and said action having been consolidated for all purposes by order of the Court upon motion of plaintiffs at the commencement of trial; and evidence both oral and documentary having been offered and received by the Court, and certain facts having been stipulated to by the parties, and the Court having heard all the testimony and all the evidence, and thereafter counsel having argued said cause, and said cause having been thereafter duly and regularly submitted to the Court for its decision, and the Court having considered said cause and having thereafter ordered judgment in favor of defendant the United States of America and against plaintiffs, and each of them, and the Court being fully advised in the premises and having considered the same, and having made, signed, and ordered filed herein its findings of Fact and Conclusions of Law which are by reference made a part hereof; now, by reason of the law and the evidence and the premises, together with the Findings of Fact and Conclusions of Law as aforesaid, it is hereby

Ordered, Adjudged and Decreed that plaintiffs Johnnie Elmease Madrigan and Fred J. Madrigan, and plaintiffs Robert Edward Madrigan and Patricia Ann Madrigan, by and through their guardian ad litem Fred J. Madrigan take nothing from defendant the United States of America by this action and that judgment be entered against plaintiffs, and each of them, and in favor of defendant the United States of America together with defendant the United States of America's costs of suit incurred herein, in the amount of $.

Done in Open Court this 17th day of February, 1958.

/s/ Willis W. Ritter
United States District Judge

[Certificate of Service omitted]

Opinion by the Court

[Transcript, pp. 833-848] * * *

The Court: I want to discuss two or three of these things with you, because you have discussed them with me and I think you are entitled to know what my views are about them. It's easy enough for a judge, you know, to say, "Judgment for the plaintiff," or "Judgment for the defendant," and "Will you, counsel, prepare the findings and conclusions and judgment?" and walk out. Now, I don't do that. I think you ought to know what my thinking is about this.

Now, to start out with, I am going to pay a little attention to Dr. Bulgrin. And that statement of his that the chances were overwhelming that Mrs. Madrigan had tuberculosis in the upper left lobe of that lung on October 24, 1951.

Now, one of the jobs of the trial judge is to pass

upon the credibility of the witnesses and what they say. And I suggest to you that at the time Dr. Bulgrin said what he did about "overwhelming," I was sitting here with my eye on him, watching him. And Dr. Bulgrin relaxed, slumped down in his chair; it was the tale end of something he had been talking about, his attitude and manner of speech were such, and the character of his statement was such, that it seemed to me that that was a rather careless thing for a well-trained, experienced doctor to say. Now, I did some compliment in the record to Dr. Hinshaw's careful statement. I refer to that and adopt it again.

Dr. Hinshaw had the bearing and demeanor of a scientist and in what he said, he expressed himself with the careful attention to detail and the thoughtful attention to his phrases, to their meaning and extent. Now, without casting any uncomplimentary suggestion upon Dr. Bulgrin, I suggest to you that the testimony of Dr. Hinshaw in my judgment is the more credible.

Now, Dr. Hinshaw did not say anything about that being overwhelming in favor of T. B. He said exactly the opposite. He said they often saw in an x-ray film, such as that of October 24th, 1951, those shadows, and I copied down what he said at the time and I have my notes here. Dr. Hinshaw said those shadows were vague and questionable evidence of any disease. Dr. Hinshaw said those shadows were faint, indefinite and inconclusive, and he further said that shadows of this kind were often seen and often disappeared. When they would not know, or caused by they knew not what. He made a general suggestion that Dr. Bulgrin had over-read that film when he talked about acid fast etiology as emphatically as he did. I don't think it is too emphatic. He said this should be considered first.

Well, as between Bulgrin's statement with reference to overwhelming and Hinshaw's extremely careful statements, I must entertain the view that the testimony of Hinshaw is the more credible.

There isn't much in the testimony of the rest of the

doctors that is too far apart, really. Of course, they all agree now that that x-ray film of October 24th, 1951 should have been followed through. There should have been more tests, there should have been more films taken, there should have been sputum tests, and the like, stomach washings. There should have been an inquiry made. Now they say that. But it is impossible now to tell that she had then without paying a great deal of attention to her history since, and it is the history since that most of those doctors were impressed with. Hinshaw took a look at that film as though he were looking at it on October 24th, 1951, and he made the remarks about it that I have read to you. Hinshaw said he would not have read that 1951 x-ray as tuberculosis. He said he would not have read that as tuberculosis.

As far as I know, nobody else suspected tuberculosis in Mrs. Madrigan until May 13, 1955 in Tokio, Japan, when she was hospitalized for a far-advanced case of tuberculosis. The first x-ray taken since October 24, 1951, was taken on May 13, 1955. So this case boils down to a rather simple problem really, and that is, did anybody fail to exercise that degree of care and skill and knowledge which medical men in this field ordinarily, usually and characteristically exercise?

We will take a look at that, and look at all the facts and circumstances in it. See if we can't paint that picture with some broad strokes and fill in the details as we go. Mrs. Madrigan appeared at the Naval Air Dispensary over at Alameda, complaining about fatigue and about fatigue connected with her feet, and she is referred to orthopedics, and this is the best evidence of what she complained about, because they sent her over to orthopedics at the Oak Knoll Hospital. When she gets through with orthopedics at Oak Knoll, she talks to Dr. Meade and Dr. Meade says, "We ought to have some surgery on your feet, Mrs. Madrigan," and she readily consents to have it done, and Meade writes up the report and says, "I think this ought to

be done, but I think the Chief of Orthopedics is not going to agree with it." The upshot is that Meade orders pre-operative procedures to be done, so that in case they go through with the surgery, they will be ready to do it.

In orthopedics they take x-rays of her feet. They send her up to radiology and they take an x-ray of her chest, and then Mrs. Madrigan comes back on the 29th of October and she is told there is not going to be any surgery, they advise a less drastic treatment for feet. Now, that x-ray film of October 24th, 1951—where is it—where is it now? Did Meade ever see it? Did Meade ever see Dr. Bulgrin's reading of it? The only evidence about that matter one way or the other is circumstantial evidence and inference. There is no direct evidence that Meade ever saw that reading. There is no direct evidence that Meade ever saw that film, and there is no direct evidence in this record that any chest man ever saw that film. Bulgrin saw it, Bulgrin read it, and we have Bulgrin's reading of it. It seems to me to be the more reasonable conjecture, more reasonable inference, if you will, to suggest that when Meade and Cruise got up to the gun on October 29th, that is when Meade and Cruise to decide whether we are going to operate or we are not going to operate, they didn't get close to it. I think what happened Cruise took the point of view that Meade said in his report, that he was likely to take, that is a very reasonable thing to assume, that Meade knew his Chief, and when Meade says, "the Chief is not going to agree with this," I think we can assume that is exactly what happened. Cruise did not agree with it. Do you mean to say if Cruise did not agree with it as an ordinary procedure on feet that he and Meade sat down and nevertheless looked at that chest x-ray, if they had it, or looked at Bulgrin's reading of it, if they had it before them? That would be a wholly unnecessary thing to do. The chest x-ray was of no importance to them. They are not going to operate.

It seems to me the only man connected with that hospital and the Navy who saw that film and saw what was in it and wrote a report about it is Bulgrin. Now, I have been asking myself this question: what was Bulgrin's duty with respect to that film? Was it Bulgrin's duty as a radiologist to go hunt Meade up and say, "look here, Meade, look at what is in this film,"—was it his duty to look up Cruise? Was it his duty to ignore both of them and hunt up the chest man at Oak Knoll. Was it his duty to go over the head of Meade and Cruise and notify Mrs. Madrigan? Well, of course, the ordinary procedure is that the man who ordered the film, if he wants to see it, will come and get it, and Bulgrin's testimony was very illuminating about their practice there. Their practice was to put the thing in a file.

Now, Bulgrin did not give us any explanation really of the delay between October 24th and November 8th or 9th, and he did not give us any explanation of the two dates November 8th and November 9th. What he did was about November 8th and November 9th, it appeared to him there must be some mistake about these dates. He said he was willing to assume November 8th was the date of the report, because that is where he had told the secretary to put that date in all cases. This is a practice he remembered and he was specific about that. When November 9th comes along, nobody knows what that amounts to. I do not believe we can decide this lawsuit on picking up little variations from the normal in matters that really don't affect the issue very much.

The only issue in this lawsuit is, Was anyone in the employ of the United States of America negligent in relation to the October 24th, 1951 film? That is to say, was there anybody there at the hospital, medical man or otherwise, who failed to exercise that degree of skill and knowledge which professional men characteristically exercise in like circumstances? It seems to me rather far to go to complain that anybody was

lacking in the exercise of ordinary and reasonable care and prudence under these circumstances. If a chest man like Hinshaw or Shipman or the Hollander who was here—I forget his name—or Dr. Wilson, had put his eye on the film in the hospital in 1951 and then had not done anything about it at all, we would have had a different problem. But this radiologist Bulgrin, it seems to me, was exercising a high degree of care, skill and knowledge which he possessed, and which radiologists characteristically possess and exercise in like situations. He read the film, he put his reading down, and then the reading went where it was supposed to go, and the film went where it was supposed to go. It seems to me the only reasonable interpretation you can put on those facts—the fact is, we do not know what happened. We have to draw inferences from what we do know. It is my judgment that there was no failure in this case on the part of anybody employed by the United States to exercise that degree of skill and care and knowledge and prudence that is ordinarily possessed and exercised by professional men, members of the profession, under similar circumstances to these.

Dr. Hinshaw went further and said he would not expect a shadow of that faintness to explain any of her symptoms of fatigue and so on, and he said that at this time, that is, on January 22nd, 1958, it is impossible to tell if her condition reflected in the October 24th, 1951 film, had anything at all to do with the far-advanced case of tuberculosis with which she was suffering in Japan in May of 1955. Dr. Hinshaw says that the alcohol and the emotional misfortunes which the poor woman has suffered were the most important causes of her tuberculosis in his judgment.

We have Dr. Bulgrin, and Dr. Bulgrin only, it seems to me, in this evidence who had that film, had that reading, and one asks himself, "What ought Bulgrin to have done?"

Well, it is clear there was no reason outside ordi-

nary medical practice, ethics and the relationship between patients and physicians for Bulgrin to have done anything but what he did. He put the reading on the jacket or had his secretary do it. He sent the original along to the secretary of the Chief of the Orthopedic Section, and what happened to it nobody knows.

I think what happened was it became unimportant to the orthopedists because they had given up the idea of surgery. So they are doing something much less drastic, and it seems to me much more sensible, than that of drastic surgery. I am borne out in that thought by the fact that there is no evidence in this record that she ever did have surgery on her feet. That condition she is apparently getting along with. It must be tolerated because there are no further complaints about that.

So again we are borne out in the inference that in the good judgment of those two doctors they gave up surgery as a possibility, and having given it up as a possibility, there was no sense at all in worrying about the pre-operative procedure, including the examination of an x-ray film. So Bulgrin, was he to go down to Mead and tell him "Look here, Mead." That isn't their practice. No doctor has testified they do that. We know they don't. Do you suppose Bulgrin would go down to Cruise, the head of the Orthopedic Department, and say, "Look here, Cruise, you must pay some attention to this." Cruise would have thrown him out. That is not the way doctors operate in a hospital. Bulgrin's job was to read those x-rays up in radiology and put them where they were accessible to the physicians, where they could be obtained for future reference by anybody who was interested in them.

The operation on the foot having fallen through, Mead and Cruise were not interested in that any longer. That seems to me to be the plain fact in this case. It seems to me to be much more reasonable.

Was it Bulgrin's duty to hunt up the chest expert

and say, "Look, see what I found"? This was the 17,299th film. 17,299 films had been taken and read in that radiology department between the first of January, 1951, and October 24, 1951. Is it their duty, these radiologists, if they see something they suspect in a film to run around to see the specialist in the field and say, "Look here, have a look at that." Of course they don't. Bulgrin acted prudently, skillfully, it seems to me. He read it, put it in a jackaet, and filed it. I think that is what happened. Perhaps Bulgrin was right and perhaps he was not right in suggesting that maybe between October 24th and November 8th or 9th the orthopedists had that film down there, that is, before he read it. I don't know whether that is what happened or not. He said that might have been an explanation but he didn't know. He did know there was some mistake about those dates, November 8th and November 9th. It couldn't be both dates. He thought the 8th was more likely the date on which the report was made and typed.

Everything in this case comes down, it seems to me, to that October 24, 1951 film, and as far as the evidence in this case goes, nobody saw that except Bulgrin, and if Mead and Cruise were giving up the operation on the feet, there wasn't any need for them to look at that at all. It had no significance. In the first place, Mead is an orthopedist, Cruise is an orthopedist, and there is some testimony in this case that neither Mead nor Cruise is competent to read that film. The only thing they could have done was to read Bulgrin's report and then do something about it, if they ever saw that report. There is no evidence in this case that they did see the report. I think the evidence is against it, really, against seeing the report, against their seeing the film, because it seems to me to be a very reasonable assumption that they had decided not to operate and they did not pay any more attention to that chest film.

Mrs. Madrigan had not complained of t.b., of course; she had symptoms that Hinshaw and all of them say

showed fatigue, but it is the symptom of a lot of other things, too. There was no suggestion by anybody back in 1951 about tuberculosis. There was no chest expert in the case on Mrs. Madrigan either at the hospital or otherwise. Certainly no chest man saw the film over at Oak Knoll, unless you call Bulgrin a chest man. Bulgrin is a radiologist. Now, while I am paying some attention to the credibility of the testimony here, examine the high degree of qualification of Dr. Hinshaw, Dr. Wilson and Dr. Kruisheer as compared with the qualifications of Bulgrin. Bulgrin is to be commended for the reading he made of that film in 1951, but Bulgrin's qualifications do not stand up enough. Bulgrin is not operating in the same league as we sometimes say, as Dr. Hinshaw, a man who for 15 years was at Mayo's Clinic in this specialization and who is the head of the department in his specialization at Stanford with long experience, who has read thousands of films like this. Hinshaw said he just did not know what was in that film of October 24, 1951. He just did not know. He did say that if he saw it, he would want to tell the patient about it. He would want to do some further procedures. Of course, at this late date there is the history of a disastrous condition, and from this point of view that film of 1951 becomes all the more suspect.

I am troubled by the fact that Mrs. Madrigan did not return. Of course, Mrs. Madrigan did not know she had tuberculosis either, if she had it at that time. Nobody knows whether she did or not. But she did not return. Now, had she returned within a month as she was directed to do, perhaps that record would have been pulled out and somebody would have paid some attention to that film. But as it turns out in this case, with Mrs. Madrigan not returning, no doctor's attention invited to the thing—where was it? Well, I think it was filed away in Radiology. That is where it was, and it would be there until some doctor called for it. He wanted to examine it and discuss

it with her. She did not come around and call to attention any condition she had after that. She just did not return.

Mead and Cruise went along in that busy hospital doing their jobs. Bulgrin went along in that busy hospital doing his job. No chest man ever saw it. No chest man ever had any duty to see it. Well, it boils down to that in my judgment.

From the point of view of hindsight, looking at it now after the terrible illness this woman has sustained, we go back and point the finger at those vague, indefinite, inconclusive, faint, to use the word Hinshaw used, shadows in the film and say, "Well, this is what she had and it exacerbated in May 1955 or shortly before."

Something has been said about the duty to notify the patient. As I view this case, Bulgrin is the only fellow who saw that film professionally. Did he have any duty to call Mrs. Madrigan's attention to it? Of course not. There is a reference to him in Radiology from Mead. His job is to send it back to Mead, if anything, or make it available for him. He said it was not his job to send it back; it was his job to put it in a file, and if Mead wanted it he would send a corpsman for it or come for it himself.

Well, in my judgment, there is no negligence on the part of anyone connected with the United States or for whom the United States is responsible. And if there were lack of ordinary and reasonable care, skill, prudence, knowledge, I would have the greatest difficulty finding that that lack of skill, if any, was connected with the far-advanced case of active pulmonary tuberculosis this woman had in May of 1955. There isn't anybody now, even with hindsight, who can say what was in that chest of hers at that time with any reasonable degree of medical certainty—anybody.

Now, it is interesting to observe here that it is the younger ones, the least experienced, and those who haven't yet developed a very high degree of care in

their observations and statements, who go the farthest in this record. Hinshaw and Shipman seem to me to come very close to stating just about all one can state concerning this evidence. I prefer to take the view that the credibility of Dr. Hinshaw's testimony here is to be preferred to the credibility of Kruisheer, the credibility of Bulgrin and the credibility of Dr. Wilson.

Dr. Wilson is a splendid man, but he is a young man. He has a wonderfully fine educational background and a good deal of experience, but I was of the opinion and am now that Dr. Wilson made of himself something of an advocate in this case, and I don't suggest anything uncomplimentary to him or to counsel in that connection. He was just very enthusiastic about those films of his. I tried very hard, and of course I am unskilled in reading x-ray films, but I tried very hard to see what they were talking about and I think I saw it. And I suggested to Dr. Wilson while we stood down on the floor and examined that film, that there was only a faint distinction between what he said was normal in the right lung and what was abnormal in the left. I said, "That's such a faint difference," and he said, "Well, that's the thing about this disease—it's that a very, very faint little difference is of such horrible significance."

Well, "horrible" is a large word, and it seems to me a little reckless word to be using in these connections. I mention that as bearing upon the credibility in weighing credibility of Wilson and Hinshaw. You didn't find any words like that in Hinshaw's testimony. He is a very careful, scientific man. He weighed what he said with extreme care.

Well, I don't know that I can spell out any more fully what I have in mind. In short, there is no negligence, and if there were, I can see no connection between the negligence, if any, and what happened to Mrs. Madrigan. And it is unnecessary to go into the damages, therefore.

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